

Federal Housing Finance Agency
Office of Inspector General



FHFA Complied with Applicable Improper Payment Requirements During Fiscal Year 2015

Audit Report • AUD-2016-003 • May 5, 2016



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Executive Summary

The Improper Payments Information Act of 2002 (IPIA), as amended by the Improper Payments Elimination and Recovery Act of 2010 (IPERA) and the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA) (collectively, IPIA, as amended), requires federal agencies periodically to review, estimate, and report programs and activities that may be susceptible to significant improper payments. The IPIA was amended by IPERA to direct federal Inspectors General to determine annually whether the agency is in compliance with the statute and to submit a report to the head of FHFA, Congressional oversight committees, the Comptroller General of the United States, and the controller of the Office of Management and Budget (OMB).

The Federal Housing Finance Agency (FHFA), through its Office of General Counsel (OGC), maintains that most requirements of the IPIA, as amended, are not applicable to FHFA because those requirements apply only to payments made with federal funds and FHFA does not finance its operations with federal funds. Nevertheless, FHFA asserts that it has put into place internal controls to achieve the intent of the IPIA, as amended. FHFA's Office of Inspector General (OIG) conducted a performance audit to assess FHFA's compliance with the IPIA, as amended, for fiscal year 2015. We found that FHFA complied with the applicable provisions of the IPIA, as amended, as well as related criteria established in OMB Memorandum M-15-02.

This audit was conducted by Tara Lewis, Audit Director, and Philip Noyovitz, Senior Auditor. We appreciate the cooperation of FHFA staff, as well as the assistance of all those who contributed to the preparation of this report, including Anya Philbert and Julio Santos.

We distributed this report to the Congress, OMB, and others and posted it at www.fhfaoig.gov.

A handwritten signature in black ink, appearing to read "Stacey Nahrwold".

Stacey Nahrwold
Acting Deputy Inspector General for Audits

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ABBREVIATIONS

AFR	Agency Financial Report
FHFA	Federal Housing Finance Agency
GAO	Government Accountability Office
IPERA	Improper Payments Elimination and Recovery Act of 2010
IPERIA	Improper Payments Elimination and Recovery Improvement Act of 2012
IPIA	Improper Payments Information Act of 2002
OGC	Federal Housing Finance Agency Office of General Counsel
OIG	Federal Housing Finance Agency Office of Inspector General
OMB	Office of Management and Budget
PAR	Performance and Accountability Report
U.S.C.	United States Code

BACKGROUND

Because federal agencies regularly make payments to program beneficiaries, grantees, vendors, and contractors, or on behalf of program beneficiaries, there is a possibility that some of these payments may be “improper” in one or more respects. To provide estimates and report improper payments by federal agencies, Congress enacted the IPIA in 2002,¹ which it amended in 2010 with the IPERA and again in 2013 with the IPERIA. The IPIA, as amended by the IPERA, requires federal agencies to periodically review, determine, estimate, and report programs and activities that may be susceptible to significant improper payments.² According to the IPIA, as amended, the term “payment” means: “[A]ny transfer or commitment for future transfer of Federal funds such as cash, securities, loans, loan guarantees, and insurance subsidies to any non-Federal person or entity or a Federal employee, that is made by a Federal agency, a Federal contractor, a Federal grantee, or a governmental or other organization administering a Federal program or activity.”³

To provide further guidance to federal agencies on the improper payments covered by the IPIA, as amended, the Office of Management and Budget (OMB) issued a memorandum in 2014 that provides a more robust definition of the term “improper” payment:

[A]ny payment that should not have been made or that was made in an incorrect amount under statutory, contractual, administrative, or other legally applicable requirements. Incorrect amounts are overpayments or underpayments that are made to eligible recipients (including inappropriate denials of payment or service, any payment that does not account for credit for applicable discounts, [footnote omitted] payments that are for an incorrect amount, and duplicate payments). An improper payment also includes any payment that was made to an ineligible recipient or for an ineligible good or service, or payments for goods or services not received (except for such payments authorized by law). In addition, when an agency’s review is unable to discern whether a payment was proper as a result of insufficient or lack of documentation, this payment must also be considered an improper payment.⁴

¹ Public Law No. 107-300, 31 U.S.C. § 3321 note.

² Public Law No. 111-204, 31 U.S.C. § 3321 note.

³ *Id.*

⁴ OMB Memorandum M-15-02, Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments* (Oct. 20, 2014) [hereinafter OMB Memo M-15-02, App. C], at Part I ¶¶ 2 and 3.

The IPIA, as amended, directs federal agencies to put into place internal controls designed to eliminate payment errors, waste, fraud, and abuse, including reducing and recapturing erroneous payments. OMB Memorandum M-15-02 establishes a four-step process for agencies to follow to identify those operations subject to the IPIA, as amended, and to design and implement appropriate internal controls to reduce the risk of improper payments:

1. Review all programs and activities and identify those that are susceptible to significant improper payments;
2. Obtain a statistically valid estimate of the annual amount of likely improper payments in programs and activities identified in Step 1;
3. Develop and implement a plan sufficient to reduce improper payments; and
4. Report annually on improper payments in its performance and accountability report (PAR) or agency financial report (AFR) to Congress.⁵

To validate the accuracy of agency reporting on improper payments in its annual PAR or AFR, the IPIA, as amended, requires Inspectors General to conduct an annual review which includes six elements:

1. A determination that the agency has published an AFR or PAR for the most recent fiscal year and posted that report and any accompanying materials required by OMB on the agency website;
2. A determination that the agency has conducted a program-specific risk assessment for each program or activity that conforms with Section 3321 note of Title 31 U.S.C. [i.e., the IPIA, as amended] (if required);
3. A determination that the agency has published improper payment estimates for all programs and activities identified as susceptible to significant improper payments under its risk assessment (if required);
4. A determination that the agency has published programmatic corrective action plans in the AFR or PAR (if required);

⁵ OMB Memo M-15-02, App. C, *supra* note 1, at 9-16. A PAR provides both financial and performance information that enables the President, the Congress, and the public to assess the performance of an agency relative to its mission and to demonstrate accountability. An AFR provides similar information, but a Performance section is not included. See OMB, Circular A-136, *Financial Reporting Requirements*, at 11-13 (Sept. 18, 2014).

5. A determination that the agency has published, and is meeting, annual reduction targets for each program assessed to be at risk and estimated for improper payments (if required and applicable); and
6. A determination that the agency has reported a gross improper payment rate of less than 10 percent for each program and activity for which an improper payment estimate was obtained and published in the AFR or PAR.⁶

Inspectors General are expected to complete their annual compliance reviews within 180 days after their respective agencies issue their PARs or AFRs and report their findings.⁷ If an Inspector General finds that an agency has not met one or more of the six elements, that agency is required by the IPIA, as amended, to submit a plan to the Congress describing the actions it will take to come into compliance.⁸ Further, OMB will notify agencies of additional required actions as needed based on the compliance level of each agency. OMB Memorandum M-15-02 provides detailed information on agency compliance planning and related efforts to become compliant.

FHFA issued its fiscal year 2015 PAR on November 16, 2015. Pursuant to the IPIA, as amended, OIG conducted this performance audit.

FACTS AND ANALYSIS

Not All IPIA Requirements Are Applicable to FHFA

In its most recent PAR, FHFA reports:

The Improper Payments Elimination and Recovery Act requires that agencies:
(1) review activities susceptible to significant erroneous payments; (2) estimate the amount of annual erroneous payments; (3) implement a plan to reduce erroneous payments; and (4) report the estimated amount of erroneous payments and the progress to reduce them.⁹

⁶ OMB Memo M-15-02, App. C, *supra* note 1, at Part II § A(3).

⁷ OMB Memo M-15-02, App. C, *supra* note 1, at Part II § A(2).

⁸ IPERA § 3(c)(1)(A), *see* 31 U.S.C. § 3321 note.

⁹ *See* FHFA, *Fiscal Year 2015 Performance and Accountability Report*, at 111 (Nov. 16, 2015).

FHFA makes no representations in this PAR that it is covered by the IPIA. Since 2012, FHFA's Office of General Counsel (OGC) has advised OIG that it has concluded that various subsections of the IPIA, as amended, are only applicable to payments made with federal funds, and that these subsections do not apply to FHFA because it is an independent regulatory agency that does not seek appropriations for its operations. As a consequence, OGC reasons that payments made by FHFA, such as payments to vendors, are not transfers of federal funds.¹⁰

Figure 1 summarizes the requirements of the IPIA, as amended, and the elements that FHFA considers inapplicable to its operations.

FIGURE 1. FHFA'S IMPROPER PAYMENTS INFORMATION ACT COMPLIANCE FOR FISCAL YEAR 2015

Compliance Element	FHFA Action
The agency has published an annual PAR or AFR for the most recent fiscal year and posted that report and any accompanying materials required under guidance of OMB on the agency website.	FHFA published its 2015 PAR and included relevant information pertaining to improper payments.
The agency has conducted a program specific risk assessment for each program or activity that conforms with the IPIA, as amended (31 U.S.C. § 3321 note) (if required).	FHFA determined that this section of the IPIA, as amended, is not applicable.
The agency has published improper payments estimates for programs and activities identified as susceptible to significant improper payments under its risk assessment (if required).	FHFA determined that this section of the IPIA, as amended, is not applicable.
The agency has published programmatic corrective action plans in its PAR or AFR (if required).	FHFA determined that this section of the IPIA, as amended, is not applicable.
The agency has published, and is meeting, improper payments reduction targets for each program assessed to be at risk and estimated for improper payments (if required and applicable).	FHFA determined that this section of the IPIA, as amended, is not applicable.
The agency has reported a gross improper payment rate of less than 10% for each program and activity for which an estimate was obtained and published in its PAR or AFR.	FHFA determined that this section of the IPIA, as amended, is not applicable.

We reviewed the information provided by FHFA's OGC, and our Office of Counsel made an independent assessment of the reasonableness of the applicable legal authorities on which it

¹⁰ See 12 U.S.C. § 4516(f).

relied. Based on its review, OIG's Office of Counsel determined that OGC's analysis is reasonable and OIG does not challenge FHFA's conclusions.

Notwithstanding the inapplicability of these various IPIA subsections, FHFA advises in its PAR:

FHFA, in the spirit of compliance and as part of a sound internal control structure, has established controls to detect and prevent improper vendor payments. FHFA has identified no activities susceptible to significant erroneous payments that meet IPIA's thresholds. Additionally, FHFA pursues the recovery of all improper payments.¹¹

To test the accuracy of this representation by FHFA, OIG reviewed relevant invoice and payment desktop procedures implemented by FHFA to mitigate the risks of fraud, misuse, and payment delinquency. We found no design flaws within the policies and procedures. We recognize that the Government Accountability Office (GAO) annually assesses, evaluates, and determines whether FHFA's internal controls over financial reporting are properly designed and operating effectively in all material respects.¹² In its report *Financial Audit: Federal Housing Finance Agency's Fiscal Years 2015 and 2014 Financial Statements*, GAO identified deficiencies in FHFA's internal controls over financial reporting. However, GAO did not consider any of these deficiencies to be material weaknesses or significant deficiencies.¹³ While GAO's audit expressed no opinion on the effectiveness of FHFA's internal controls related to improper payments or FHFA's compliance with the IPIA, as amended, GAO did not identify any issues related to the design and effectiveness of FHFA's invoice and payment process control, and made no findings relating to the accuracy of disbursements.

¹¹ See FHFA, *Fiscal Year 2015 Performance and Accountability Report*, at 111 (Nov. 16, 2015).

¹² GAO's audit was not designed to express an opinion on the effectiveness of FHFA's internal controls related to improper payments or FHFA's compliance with the IPIA, as amended, specifically, but rather it was intended to assess controls over financial reporting generally. Consequently, GAO's audit may not identify all deficiencies in FHFA's internal controls over financial reporting that are less severe than a material weakness. According to the American Institute of Certified Professional Accountants' *Professional Standards*, AU-C § 265.07, 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, to prevent, or detect and correct, misstatements on a timely basis.

¹³ *Id.* A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

CONCLUSION.....

OIG concludes that FHFA complied with the applicable statutory improper payment requirements, as well as related criteria established in the related OMB Memorandum M-15-02 for FY 2015. As to the specific requirements of the IPIA, as amended, that FHFA has opined are non-applicable, OIG does not contest FHFA's interpretation.

OIG acknowledges that FHFA is acting to achieve the intent of the IPIA, as amended, and the related OMB guidance, regardless of its determination that it is not required to do so. Specifically, in the spirit of compliance and as part of a sound internal control structure, FHFA has established controls to detect and prevent improper vendor payments, such as invoice payment processing procedures that include detailed instructions on properly verifying the accuracy of vendor invoice amounts prior to payment.

OBJECTIVE, SCOPE, AND METHODOLOGY

OIG's audit objective was to determine whether FHFA is in compliance with the IPIA, as amended, as well as criteria established in OMB Memorandum M-15-02. This audit covered FHFA's efforts to comply with the IPIA, as amended, and OMB Memorandum M-15-02 requirements to detect, prevent, and report improper payments during FHFA's fiscal year period October 1, 2014, to September 30, 2015. To accomplish the audit objective, OIG reviewed applicable statutes, executive orders, and other related compliance requirements on improper payments reviewed in various GAO audit reports; met with key FHFA officials; obtained sufficient and appropriate evidence on compliance actions taken (e.g., confirmed that FHFA's 2015 PAR was posted to its website and reviewed OGC correspondence); and reviewed and assessed improper payment element requirements and related activities. OIG conducted its field work between December 2015 and April 2016 and issued its report in accordance with OMB requirements (i.e., within 180 days of publication of FHFA's PAR).

OIG's review of FHFA's internal controls designed to comply with the IPIA, as amended, was limited. OIG reviewed FHFA's written documentation and legal opinions related to its determination that the IPIA, as amended, provisions—and therefore most improper payment compliance elements—are not applicable to FHFA. OIG also reviewed IPERIA to ascertain whether FHFA is subject to the Act's requirements. FHFA determined that IPERIA—like IPIA and IPERA—does not apply to FHFA because the Agency does not utilize appropriated funds. For this reason, the funds used by FHFA to make payments do not qualify as federal funds under applicable law, and therefore most of the various improper payments requirements set forth by these statutes are not triggered. OIG confirmed the posting of the 2015 PAR and accompanying materials on FHFA's external website in accordance with OMB guidance and the inclusion of appropriate language that FHFA established and maintains internal control procedures for handling improper payments.

OIG conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that audits be planned and performed to obtain sufficient, appropriate evidence to provide a reasonable basis for OIG's findings and conclusions based on the audit objective. OIG believes that the evidence obtained provides a reasonable basis for the conclusions included herein, based on the audit objective.

APPENDIX A

FHFA's Comments



Federal Housing Finance Agency

MEMORANDUM

TO: Stacey Nahrwold, Senior Attorney Advisor, Acting Deputy Inspector General-Audits
(MK)

FROM: Mark Kinsey, Chief Financial Officer

SUBJECT: Audit: FHFA Complied with Applicable Improper Payment Requirements During Fiscal Year 2015

DATE: April 26, 2016

Thank you for the opportunity to respond to the Federal Housing Finance Agency Office of Inspector General's (OIG) draft audit report titled *FHFA Complied with Applicable Improper Payment Requirements During Fiscal Year 2015* (Report). The Report presents the results of the OIG's performance audit to assess FHFA's compliance with the Improper Payments Information Act of 2002 (IPIA), as amended.

I am pleased that the OIG concluded that FHFA complied with the applicable provisions of the IPIA, as amended, as well as criteria established in the OMB Memorandum M-15-02. The Report recognized that in the spirit of compliance and as part of a sound internal control process, FHFA has established controls to detect and prevent improper vendor payments and that FHFA's invoice payment processing procedures include detailed instructions on properly verifying the accuracy of vendor invoice amounts prior to payment.

I would like to acknowledge the dedicated OIG staff that worked with FHFA during this audit.

If you have any questions relating to our response, please do not hesitate to call me at (202)649-3780.

Non-Public

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