Office of the Chief Financial Officer, Washington, DC

Additional Details To Supplement Our Fiscal Years 2018 and 2017 (Restated) U.S. Department of Housing and Urban Development Financial Statement Audit

Office of Audit, Financial Audits Division
Washington, DC

Audit Report Number: 2019-FO-0003
November 15, 2018

To: Irving Dennis, Chief Financial Officer, F

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From: Thomas R. McEnanly, Director, Financial Audits Division, Washington DC, GAF

Subject: Additional Details To Supplement Our Fiscal Years 2018 and 2017 (Restated) U.S. Department of Housing and Urban Development Financial Statement Audit

Attached is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) additional details to supplement our audit of HUD's internal controls over financial reporting and compliance with applicable laws, regulations, contracts and grant agreements.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, section 8M, requires that OIG post its publicly available reports on the OIG website. Accordingly, this report will be posted at http://www.hudoig.gov.

If you have any questions or comments about this report, please do not hesitate to call me at 202-402-8216.

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Highlights

What We Audited and Why

We are required to audit the consolidated financial statements of the U.S. Department of Housing and Urban Development (HUD) annually in accordance with the Chief Financial Officers Act of 1990 as amended. This report supplements our independent auditor's report on the results of our audit of HUD's principal financial statements for the fiscal years ending September 30, 2018 and 2017 (restated), related to HUD's internal controls and compliance with applicable laws, regulations, and governmentwide policy requirements and provisions of contracts and grant agreements.

What We Found

We issued a disclaimer of opinion on HUD's consolidated financial statements for fiscal years 2018 and 2017 (restated) due to severe weaknesses in HUD's internal controls over financial reporting. This report provides additional details on three material weaknesses, three significant deficiencies, and five instances of noncompliance with applicable financial management laws and regulations. We also cited another matter that warranted attention by management. Details of the results of our audit of HUD's component entities, the Federal Housing Administration and Government National Mortgage Association, can be found in separate audit reports.

Primarily, HUD (1) had errors in its fiscal year 2018 yearend financial statements provided for audit and fiscal year 2017 financial statements and notes required restatement; (2) third quarter financial statements and note disclosures were misstated and missing required information; (3) inadequately accounted for assets, liabilities, and budgetary resources in accordance with U.S. generally accepted accounting principles (GAAP); (4) lacked adequate financial management systems to ensure accurate and reliable financial reporting; (5) continued to experience shortcomings in financial management; and (6) reported significant amounts of invalid obligations. These conditions were caused by (1) ineffective internal controls over financial reporting, (2) continued reliance on legacy financial management systems that did not always comply with the Federal Financial Management Improvement Act of 1996, and (3) continued weaknesses in HUD's financial management governance structure.

What We Recommend

We recommend that HUD (1) properly account for all financial transactions in accordance with GAAP, (2) improve internal controls over the financial reporting process, (3) develop and implement policies and procedures, and (4) deobligate up to $113.4 million in invalid or inactive obligations.

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Background and Objective

We were engaged to audit HUD's principal financial statements in accordance with Government Auditing Standards and the requirements of Office of Management and Budget (OMB) Bulletin 19-01, Audit Requirements for Federal Financial Statements, and as required by the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994. The objective of our engagement was to express an opinion on the fair presentation of these principal financial statements. This report provides additional details to supplement our independent auditor's report on HUD's consolidated financial statements for fiscal years 2018 and 2017 (restated).

In planning our audit of HUD's principal financial statements, we considered internal controls over financial reporting and tested compliance with selected provisions of applicable laws, regulations, and government policies that may materially affect the consolidated principal financial statements. Providing an opinion on internal controls or compliance with selected provisions of laws, regulations, and government policies was not an objective, and, accordingly, we do not express such an opinion.

Management is responsible for

- Preparing the financial statements in conformity with accounting principles generally accepted in the United States of America.
- Establishing, maintaining, and evaluating internal controls and systems to provide reasonable assurance that the broad objectives of the Federal Financial Management Improvement Act of 1996 (FFMIA) are met.
- Complying with applicable laws, regulations, contracts, and grant agreements.

This report is intended solely for the use of HUD management, OMB, and Congress. However, this report is a matter of public record, and its distribution is not limited.

Report on Internal Controls Over Financial Reporting

Material Weaknesses

Finding 1: HUD's Financial Reporting Controls Were Not Fully Effective To Ensure Complete and Accurate Consolidated Financial Statements and Notes

In fiscal year 2018, HUD made significant improvements to its controls over financial reporting; however, there were still shortcomings in its internal control system. Specifically, HUD's internal control system did not have effective controls to reasonably ensure that it gathered and accurately included all necessary information from its component entities, program offices, and the Office of General Counsel (OGC) into its consolidated financial statements. Further, neither Ginnie Mae nor HUD had adequate controls in place to ensure that Ginnie Mae's accounting system produced accurate budgetary balances. Due to ineffective controls, HUD's fiscal year 2018 financial statements and notes provided for audit contained material errors that were not detected and fiscal year 2017 financial statements and notes required restatement. Additionally, HUD's third quarter fiscal year 2018 financial statements and notes were misstated and missing required information. As a result, stakeholders did not have accurate and complete information required by Federal generally accepted accounting principles (GAAP), and OMB regulations. Further, the control weaknesses that led to these misstatements increased the risk of errors and may cause other misstatements in HUD's yearend financial statements that were not detected and corrected within the yearend reporting timeframes.

Shortcomings in HUD's Financial Reporting Controls

In prior years, we reported on pervasive weaknesses in HUD's internal controls over financial reporting. First, in fiscal year 2015, we reported on pervasive weaknesses in Ginnie Mae's internal controls over its budgetary accounting which caused material misstatements.[1] Then, in fiscal year 2016, we reported on pervasive weaknesses in all elements of HUD's internal controls over financial reporting.[2] Specifically, we reported that HUD's Office of the Chief Financial Officer (OCFO) failed to design and implement an adequate system of internal controls to mitigate the challenges and risks in its complex financial reporting process. These challenges and risks were increased with the transition of HUD's legacy general ledger application to an

[1] Audit report 2016-FO-0003- Additional Details to Supplement Our Fiscal Years 2015 and 2014 (Restated) U.S Department of Housing and Urban Development Financial Statement Audit, issued November 18, 2015.

[2] Audit report 2017-FO-0003- Additional Details to Supplement Our Fiscal Years 2016 and 2015 (Restated) U.S Department of Housing and Urban Development Financial Statement Audit, issued November 15, 2016.

enterprise resource management application housed in a Federal shared service provider (FSSP).[3] With the change to an FSSP, HUD needed to completely redesign its processes and procedures to (1) compliment controls in place at the FSSP, (2) design and implement new controls over financial reporting within HUD, and (3) identify and mitigate new emerging risks as a result of the changes. However, in fiscal year 2017, HUD still had not changed its internal control system to accommodate its new financial reporting environment.

In fiscal year 2018, we noted progress in all areas; however, shortcomings still existed. First, Ginnie Mae implemented automated controls over its budgetary accounting. However, its controls were not sufficiently robust to prevent and detect errors, and HUD OCFO's controls over component entity data did not detect errors. Second, HUD's Financial Reporting Division (FRD) made significant improvements in its processes and procedures to establish appropriate controls in its new environment. However, there were still gaps in its system of controls related to processes that cannot be automated but, instead, require timely and effective communication between OCFO and HUD's program and legal offices and component entities to report accurate information. Specifically, we found the following:

> *Controls over Ginnie Mae's budgetary accounting were not adequate* - In fiscal year 2015, Ginnie Mae inappropriately closed U.S. Standard General Ledger (USSGL) account 4610 (allotments) into 4450 (unapportioned authority) before yearend closing,[4] which resulted in material misstatements and contributed to HUD's fiscal year 2016 material weakness over financial reporting. To address this issue, Ginnie Mae (1) automated the process, which included system controls, and (2) performed a tie point analysis to identify issues in its data. However, the system controls were not configured properly and the analysis did not include a tie point to ensure accounts 4610 and 4450 were accurate. Further, while HUD performed a fluctuation analysis on some of the line items on Ginnie Mae's statement of budgetary resources, it did not perform an analysis on the unapportioned and apportioned line items.[5] Consequently, in fiscal year 2018, Ginnie Mae's system also closed these accounts before yearend closing and neither Ginnie Mae's nor HUD's financial reporting internal controls detected the errors.
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> *The current certification process is not fully effective* – To ensure that HUD accurately presented its component entities' (Federal Housing Administration (FHA) and Government National Mortgage Association (Ginnie Mae)) data in the consolidated financial statements, it implemented a certification process in its new financial reporting system (OneStream). The certification process was also used by HUD's FRD director, the Assistant Chief Financial Officer (ACFO) for Accounting, and the Deputy Chief Financial Officer (DCFO). While certification is an important control, it alone cannot

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3 In fiscal year 2016, HUD transitioned to an FSSP, the U.S. Department of the Treasury's Bureau of Fiscal Services, Administrative Resource Center (ARC), which included the migration of its general ledger to Oracle Federal Financials and many of its financial reporting processes.

4 The USSGL states that agencies close these accounts in the yearend closing process, not before issuance of its yearend statements.

5 Account 4610 crosswalks to the Apportioned, Unexpired Account line item and account 4450 crosswalks to the Unapportioned, Unexpired line item.

ensure accuracy. In HUD's third quarter reporting, there were two instances in which errors were identified, but the approving officials certified without correcting the issues. First, for the status of fund balance with Treasury in note 3, FHA certified that its information was presented accurately in OneStream, although it did not agree with FHA's presentation in its stand-alone financial statements. HUD also knew that there were differences between FHA's and HUD's crosswalk; however, it certified without confirming that the issues had been resolved. Second, HUD's internal controls identified a difference in the direct loans and loan guarantees balance between the 2017 financial statements and the amounts presented for 2017 in the 2018 comparative balance sheet. However, since the issue and resolution were not documented, the statements were certified by HUD's FRD director, the ACFO, and the DCFO before its correction.

Historically, gathering information from its component entities has been HUD's greatest financial reporting challenge. To mitigate this risk, HUD and FHA should have implemented additional control activities to supplement the certification process. However, neither HUD nor FHA validated the FHA portion of HUD's Note 3, Fund Balance with Treasury, with FHA's stand-alone financial statements and note disclosures before certification. While FRD's final standard operating procedures include procedures for verifying against component entity stand-alone notes, the draft version did not. FRD did not complete the final version of the standard operating procedures until after the third quarter statements and notes were prepared.

OCFO's process for gathering information on HUD's contingent liabilities had weaknesses – FRD's standard operating procedures do not include procedures for inquiring on the status of HUD's contingent liabilities. Instead, FRD relied solely on the legal representation letter from OGC, which is prepared for the purposes of the financial statement audit and not available in time for third quarter financial reporting. HUD's FRD did not have the interim legal representation letter in time to prepare HUD's third quarter statements and notes. Therefore, it relied on the 2017 final legal representation letter and a verbal update performed for the third quarter, which was not documented. Additionally, FRD's review of the 2017 final legal representation letter was not thorough. By not reviewing all elements of the letter, FRD did not realize that as of September 30, 2017, final judgement had occurred for one case and it should not have been included as a contingent liability in fiscal year 2017.

OCFO's process for gathering narrative information needs improvement – To accurately complete the narrative sections of the notes, a comprehensive working knowledge of HUD's programs is required. FRD's standard operating procedures include the following statement regarding updating the note narrative: "Reviews the consolidated Note Narrative; update if needed and ensure it agrees with HUD operations, Note Table amounts and applicable Financial Statement Line Item." However, there are no specific details on how to ensure that it agrees with HUD operations.

OCFO's processes and procedures for gathering and allocating administrative cost information had weaknesses – OCFO's processes and procedures for cost accounting and allocation of administrative funds did not fully comply with the Federal accounting standards and other regulations. Specifically, HUD did not have processes and procedures to accurately gather all cost data or appropriately allocate costs. First, there were no accounting policies and procedures between OCFO and FHA to ensure that costs were allocated in a consistent and accurate manner. Second, HUD did not consider allocating costs to Ginnie Mae. Third, HUD allocated most of its general service costs using the indirect approach but did not have a method to verify the assumptions used. Lastly, HUD's allocation of information technology (IT) costs did not sufficiently allocate direct costs to the program activities.

HUD's Fiscal Year 2018 Financial Statements and Notes Provided for Audit Contained Material Errors and its Fiscal Year 2017 Financial Statements and Notes Required Restatement

The weaknesses in HUD's financial reporting controls discussed above resulted in material errors that HUD did not detect in its fiscal year 2018 financial statements and notes provided for audit, and the need for restatement of its fiscal year 2017 financial statements and notes. Specifically, we found the following:

Ginnie Mae's budgetary accounting - The premature closing of account 4610 into account 4450 overstated and understated HUD's unapportioned and apportioned line items by $2.8 billion, respectively, on HUD's fiscal year 2018 consolidated statement of budgetary resources. It also overstated and understated the unavailable and available balances in HUD's Note 3- Fund Balances with Treasury by $2.8 billion, respectively. Upon identifying the error, we informed Ginnie Mae, who provided corrections to HUD for consolidation into its statement of budgetary resources and Note 3. HUD subsequently revised its financial statements and notes prior to publishing them in its Agency Financial Report.

HUD's cost allocation process – HUD's fiscal year 2017 financial statements misallocated costs totaling $174 million between FHA and Non-FHA programs. As a result, HUD restated its fiscal year 2017 statement of net cost to correct $174 million in understatements and overstatements between FHA and Non-FHA programs, respectively. Further, HUD's financial statements are at risk of additional misstatements since Ginnie Mae was not allocated any portion of the administrative costs included in the cost allocation, the assumptions used in the indirect cost allocation were not validated, and IT costs were not appropriately allocated to programs.

HUD's contingent liabilities – HUD's fiscal year 2017 financial statements were misstated due to the improper accounting for HUD's commitments and contingencies. HUD's fiscal year 2017 financial statements included one case that was settled in fiscal year 2017. Since this case was settled and the U.S. Department of the Treasury's Judgement Fund was determined to be the source of payment in fiscal year 2017, this no longer represented a contingent liability in fiscal year 2017.[6] Therefore, the Commitments and Contingencies and Other Liabilities line items on HUD's fiscal year 2017 balance sheet were both overstated by $136.7 million.

HUD's status of fund balance with treasury – The status of fund balance with Treasury section of HUD's fiscal year 2017 Note 3, Fund Balance with Treasury, was misstated. During our fiscal year 2017 financial statement audit, we noted issues with this note, which we communicated in our internal control report and as a basis of disclaimer in the Independent Auditor's Report.[7] HUD recalculated its status of fund balance with Treasury in its fiscal year 2017 note and determined that restatement was necessary. It restated the available, unavailable, and obligated not yet disbursed balances by $476 million, $75 million, and $551 million, respectively.

HUD's Third Quarter Fiscal Year 2018 Consolidated Financial Statements Were Misstated and Missing Information

Due to the weaknesses in HUD's financial reporting controls noted above, HUD's third quarter fiscal year 2018 consolidated financial statement and note disclosures contained errors as well, and the narratives were incomplete. Specifically, we found the following:

HUD's status of fund balance with Treasury – In addition to the errors in HUD's fiscal year 2017 statements, FHA's status of fund balance with Treasury in HUD's fiscal year 2018 third quarter consolidated financial statement note disclosure, note 3, was not accurately reflected. Specifically, the available, unavailable, and obligated balance not disbursed in HUD's Note 3, Fund Balance with Treasury, were misstated by $11.9 billion, $12.9 billion, and $1 billion, respectively.

Ginnie Mae's fiscal year 2016 restatement – The impact of Ginnie Mae's 2016 restatement was not accurately presented in the 2017 portion of HUD's comparative consolidated financial statements. The U.S. Department of the Treasury's Bureau of Fiscal Services, Administrative Resource Center (ARC), restated the Direct Loans and Loan Guarantees financial statement line item instead of the Other Non-Credit Reform financial statement line item. As a result, the Direct Loans and Loan Guarantees and Other Non-Credit Reform financial statement line items on the balance sheet were overstated and understated by $145 million, respectively.

HUD's contingent liabilities – The errors identified in HUD's fiscal year 2017 financial statements, the Commitments and Contingencies and Other Liabilities financial statement line items described above, carried over into HUD's third quarter fiscal year 2018 financial statements and did not accurately reflect HUD's contingent liabilities. Further,

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[6] Interpretation of Federal Financial Accounting Standards 2 states that once a court judgement is assessed against a Federal entity and the Judgement Fund is determined to be the appropriate source for the payment, the liability should be removed from the financial statements of the entity.

[7] 2018-FO-0005, HUD's Fiscal Years 2017 and 2016 (Restated) Consolidated Financial Statements Audit, issued November 16, 2018

the line items inappropriately included accruals for one case with a remote chance of an unfavorable outcome. As a result, the Commitments and Contingencies and Other Liabilities financial statement line items on the balance sheet were both overstated by $192 million. HUD's Note 16, Contingencies, also did not properly disclose five cases in which the chance of an unfavorable outcome was reasonably possible.

HUD's direct loans and loan guarantees – HUD's Note 7, Direct Loans and Loan Guarantees, did not adequately include narrative information required by OMB Circular A-136 and needed for stakeholders with an understanding of HUD's loans and loan guarantees. First, there were no program descriptions or any other required narratives for several of HUD's loan and loan guarantee programs.[8] Second, the note did not include disclosures related to foreclosed-on property.

Disclosure of HUD's estimates – HUD's notes were missing necessary information that stakeholders need to understand HUD's estimates. First, HUD's Note 10, PIH [Office of Public and Indian Housing] Prepayments, did not provide full disclosure of the PIH Prepayment financial statement line item, which we also reported in our fiscal year 2017 internal control report. For example, there was no information on (1) how the estimate was determined, (2) why the estimate was needed, (3) the risks associated with the estimate, or (4) the magnitude of the disbursements and expenses used in the calculation. Further, Note 1, Summary of Significant Accounting Policies, states that PIH prepares this estimate, when it was actually prepared by OCFO. Second, HUD's Note 1, Summary of Significant Accounting Policies, did not provide full disclosure of the underlying methods, assumptions, and risks associated with the Accrued Grant Liabilities financial statement line item. Such information is relevant to the user and necessary to provide a reliable representation of the line item.

Conclusion

HUD's internal control system for financial reporting did not include adequate controls to reasonably ensure that it gathered and accurately included all necessary information from its component entities, program offices, and the Office of Legal Counsel. Further, neither Ginnie Mae nor HUD had adequate controls in place to ensure that Ginnie Mae's accounting system produced accurate budgetary balances. Without effective controls, HUD's fiscal year 2018 financial statements and notes provided for audit contained material errors that it had not detected and its fiscal year 2017 financial statements and notes required restatement. Lastly, HUD's third quarter fiscal year 2018 financial statements and notes were misstated and missing information. As a result, stakeholders did not have accurate and complete information required by Federal GAAP and OMB regulations. Further, the control weaknesses that led to these

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[8] There was no narrative information on the Office of Community Planning and Development (CPD) Revolving Fund, the Section 108 loan guarantees, the Indian Housing Loan Guarantee Fund, the Loan Guarantee Recovery Fund, the Native Hawaiian Housing Loan Guarantee Fund, the Title VI Indian Housing Loan Guarantee Fund, the Green Retrofit Direct Loan Program, or the Emergency Homeowners' Loan Program. For the Flexible Subsidy Fund and the Housing for the Elderly and Disabled program, some information was provided in the narrative about HUD's methodology for calculating the allowance for loss; however, no descriptions of the programs were included.

misstatements increased the risk of errors and may cause other misstatements in HUD's yearend consolidated financial statements that were not detected and corrected within the yearend reporting timeframes.

Recommendations

We recommend that the Chief Financial Officer

1A. Develop and implement a procedure to ensure that all differences identified during financial statement and note validations are corrected before certification.

1B. Develop and implement a process that ensures the routine collection of information needed to accurately complete the narratives required according to GAAP and OMB Circular A-136.

1C. Develop and implement a procedure to ensure that HUD's quarterly consolidated financial statements accurately reflect HUD's current contingent liabilities resulting from pending or threatened litigation or unasserted claims.

1D. Restate the following in HUD's fiscal year 2017 consolidated financial statements: (1) Note 3, Fund Balance with Treasury, so that it is comparable to HUD's new status of fund balance with Treasury presentation, (2) the statement of net cost by reducing the administrative costs for non-FHA programs by $174 million, and (3) the balance sheet to correct the $136.7 million misstatements in the Commitments and Contingencies and Other Liabilities line items. If a partial restatement or no restatements are made, OCFO should provide justifications and support for the decisions.

1E. In consultation with the Office of Housing FHA Comptroller, develop and establish internal controls to ensure periodic communications for assessing and agreeing to the cost allocation accounting policies and procedures.

1F. Develop and implement a cost allocation methodology that includes all HUD programs and components, including Ginnie Mae, in the distribution of administrative costs.

1G. In consultation with the Office of Chief Human Capital Officer (OCHCO), develop and establish an activity-based costing process to validate the accuracy of factors used to allocate personnel and other administrative costs to each program and ensure that the validation is performed annually.

1H. In collaboration with the Office of the Chief Information Officer (OCIO), implement an improved cost allocation methodology for IT cost based on direct costs used by the programs.

1I. Determine whether HUD's FSSP, ARC, has resources available to enhance HUD's cost allocation methodology to identify, trace, and allocate costs directly to program activities periodically and at yearend.

1J. Develop and implement a procedure that (1) detects significant fluctuations or discrepancies in Ginnie Mae's budgetary data, (2) investigates the fluctuation or discrepancy to determine whether an error has occurred, and (3) performs corrections as needed, in a timely manner.

We recommend that the Deputy Assistant Secretary for the Federal Housing Administration

1K. Develop and implement a procedure to verify all information presented in HUD's consolidated financial statement note disclosures with its standalone note disclosures before certifying HUD's statements and notes.

We recommend the Acting Chief Financial Officer for Ginnie Mae

1L. Revise its quarterly tie point analysis to include a check for all of its budgetary accounts.

Finding 2: HUD's Accounting Did Not Always Comply With GAAP

HUD did not properly account for or have adequate support for all of its assets, liabilities, and budgetary resources. Specifically, HUD did not (1) use an appropriate method to commit and disburse fiscal year 2014 and prior obligations for the Office of Community Planning and Development' (CPD) formula grant programs; (2) account for the obligation and disbursement of funds from the Disaster Relief Appropriations Act, 2013, in accordance with GAAP; (3) properly account for its property, plant, and equipment; (4) adequately validate its accrued grant liabilities estimates; (5) accurately recognize receivables from sustained audit findings; (6) recognize prepayments for funds advanced to its Indian Housing Block Grant (IHBG) grantees for investments; (7) use complete and accurate data to estimate HUD's PIH prepayment; or (8) recognize all financial events resulting from PIH's cash management process. These deficiencies occurred because of (1) continued weaknesses in HUD's internal controls, (2) a lack of communication between OCFO and the program offices, and (3) insufficient information systems. As a result, several financial statement line items were misstated, were at risk of misstatement, or could not be audited as of September 30, 2018.

HUD Did Not Use an Appropriate Method To Commit and Disburse Fiscal Year 2014 and Prior Obligations for CPD's Formula Grant Programs

CPD's formula grant program accounting continued to depart from GAAP because of its use of the first in, first out (FIFO) method[9] for committing and disbursing obligations. In fiscal year 2016, CPD eliminated the FIFO method for commitments and disbursements of fiscal year 2015 and forward grants; however, the change was not applied to fiscal year 2014 and prior grants.

During fiscal years 2018 and 2017, $859.6 million and $1.5 billion, respectively, in disbursements were susceptible to the FIFO method and were reported in HUD's consolidated financial statements. Also during this time, $1.1 billion and $1.5 billion, respectively, in undisbursed obligations were impacted. These material amounts, which impact the combined statement of budgetary resources and consolidated balance sheet, were not presented in conformity with GAAP.

Since 2013, we have reported that the information system used, the Integrated Disbursement Information System (IDIS) Online, a grants management system, was not designed to comply with Federal financial management system requirements. For fiscal year 2014 and prior formula grants, IDIS Online continued to have inadequate budget controls and disregarded

[9] The Federal Accounting Standards Advisory Board (FASAB) Handbook defines FIFO as a cost flow assumption. The first goods purchased or produced are assumed to be the first goods sold (FASAB Handbook, Version 17, Appendix E: Consolidated Glossary, page 32, dated June 2018). In addition, the Financial Audit Manual states that the use of "first-in, first-out" or other arbitrary means to liquidate obligations based on outlays is not generally acceptable (GAO-PCIE (U.S. Government Accountability Office-President's Council on Integrity and Efficiency) Financial Audit Manual, Internal Control Phase, Budget Control Objectives, page 395, F-3). In the context of HUD's use of this method, the first funds appropriated and allocated to the grantee are the first funds committed and disbursed, regardless of the source year in which grant funds were committed for the activity.

U.S. Standard General Ledger (USSGL) attributes at the transaction level when making commitments and disbursements. This issue resulted in a departure from Federal GAAP, noncompliance with budgetary internal control requirements, and noncompliance with FFMIA. In addition, our review of HUD's unpaid obligations identified 32 grants with $150.5 million remaining as inactive.[10] CPD stated that these obligations were subject to FIFO and needed to be retained; however, due to the effects of FIFO, it could not be determined whether these obligations were still valid as of September 30, 2018.

The inability of IDIS Online to provide an audit trail of all financial events affected by the FIFO method prevented the direct effects of FIFO on HUD's consolidated financial statements from being quantified. However, because of the amount and pervasiveness of the funds susceptible to the FIFO method and the noncompliant internal control structure in IDIS Online, the combined statement of budgetary resources and the consolidated balance sheet were materially misstated.

HUD Did Not Account for Disaster Recovery Grants in Accordance With GAAP, and ADA Violations and Improper Payments May Have Occurred

A separate program audit, performed to determine whether CPD monitored and ensured that grantees complied with the 24-month expenditure requirement in the Disaster Relief Appropriations Act, 2013, identified issues with the recording of grants in the Line of Credit Control System (LOCCS) and the grantees' recording of expenditures in the Disaster Recovery Grants Reporting (DRGR) system. Specifically, we found (1) $160 million in expenditures that exceeded grant round obligations, (2) $435 million in revised and completed transactions that occurred before a grant round's obligation and after the 24-month expenditure requirement, and (3) revised and completed transactions totaling $497 million made more than a year after the original voucher entry. These issues occurred because of systemic weaknesses in DRGR and CPD's incorrectly allowing grantees to account for Community Development Block Grant Disaster Recovery funds in a cumulative manner and make transfers between rounds that had overlapping obligation periods, regardless of the date on which the grantee incurred the costs. Additionally, although LOCCS has an expiration date field, CPD's use of a single grant with many amendments in LOCCS prevented that field from being used as the grantee's single grant had multiple rounds, each of which had its own statutory expenditure deadline. The system and process weaknesses identified within DRGR resulted in noncompliance with the three section 803(A) elements of FFMIA. The noted issues also led to departures from GAAP, potential Antideficiency Act (ADA) violations, and improper payments. Additionally, HUD's unobligated balances and related line items reported in the Statement of Budgetary Resources may be misstated. OCFO had agreed to investigate the possible ADA violations, and an investigation was ongoing as of the date of this report.

HUD Did Not Properly Account for Its Property, Plant, and Equipment

As reported since fiscal year 2016, HUD continued to be unable to account for its property, plant, and equipment, including leasehold improvements and internal use software, necessary to

[10] An obligation was considered inactive if it did not have a disbursement against it for the last 2 fiscal years.

comply with Federal accounting standards.[11] We reported that HUD's capitalized costs of internal use software and software licenses with a carrying value of $335.4 million were unsupported by an adequate detailed subsidiary ledger of individual assets and balances. Further, we found that assets were not recorded because HUD had not completed its inventory of commercial-off-the-shelf software licenses to determine and record the capitalized cost and amortization. In our fiscal year 2017 audit, we reported that HUD did not recognize and properly account for at least $61.5 million in capitalized leasehold improvements and $4.7 million in capital improvement projects for the HUD headquarters building. These conditions remained outstanding, causing OCFO to represent to us that HUD's Property, Plant, and Equipment financial statement line item would be out of scope for the fiscal year 2018 audit. As a result, HUD's property, plant, and equipment balances of $335.4 million[12] reported on the financial statements remained unsupported as of September 30, 2018, and we were not able to express an opinion on this balance.

For more than a decade, OCFO, OCIO, and the Office of Administration (OA) have not had a reliable and integrated asset management system. Complementary controls and procedures to share and document acquisition and software cost information among stakeholders were not consistently followed, and oversight from senior management was not performed to detect and correct deficiencies. In fiscal year 2018, OCFO agreed, took responsibility for the prior-year recommendations, and developed corrective action plans with an expected date for full implementation in fiscal year 2019.

HUD's Grant Accrual Liabilities Validation Process Needs Improvement

As we first reported in fiscal year 2014,[13] CPD lacked an adequate validation process for its estimated accrued grant liabilities. For fiscal years 2018 and 2017, CPD reported accrued grant liabilities of $1.2 billion and $2.2 billion, respectively, which accounted for 77 and 87 percent of HUD's total accrued grant liabilities, respectively. In fiscal year 2017, OCFO took responsibility for completing a validation of CPD's grant accrual estimate. As a result of internal control deficiencies discussed below, OCFO did not adequately validate CPD's estimated accrued grant liabilities.[14]

OCFO's contractor developed a methodology to validate CPD's grant accrual estimates, which required the collection of grantee data. Due to the lack of relevant data available from grantee reporting,[15] OCFO conducted a survey to obtain grantee expenditure data for the statistical

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11 Statement of Federal Financial Accounting Standards (SFFAS) 6: Accounting for Property, Plant, and Equipment and SFFAS 10: Accounting for Internal Use Software

12 The $335.4 million in property, plant, and equipment are from HUD and FHA programs and excluded the Ginnie Mae property, plant, and equipment financial statements balances.

13 Audit Report 2015-FO-0004, Fiscal Years 2014 and 2013 Consolidated Financial Statements Audit, issued March 6, 2015

14 In accordance with the requirements of FASAB Federal Financial Accounting Technical Release 12, Accrual Estimates for Grant Programs

15 CPD implemented a systematic waiver, which allows its grantees the option to not provide the Federal Financial Report (Standard Form 425).

validation model. The survey required that grantees certify the data provided. However, OCFO did not request documentation from the grantees to support the amounts that they were certifying. Additionally, the guidance HUD provided to the grantees on how to complete the survey was limited.[16] Based on our statistical sample of 64 survey responses, we found that 22 of the 64 responses did not have sufficient documentation to support the certified responses. After extrapolating the results to the universe of 441, we determined that at least 110 records, or 25.13 percent of all survey responses, were not supported. Additionally, instead of a liability, five grantees reported holding cash advanced from HUD. These advances were included in the validation model, which was not designed to incorporate advances. HUD did not record a corresponding advance in its financial statements. We also noted in our sample of 64 responses that 11 grantees submitted an updated survey letter with revised amounts, indicating that what was previously certified to OCFO and included in the validation model was incorrect.

Although CPD and OCFO had made significant improvements in the area of grant accrual validation, the issues noted above prevented OCFO from reasonably ensuring that the amounts included in its statistical validation model and the model results were accurate. Therefore, the validation model included data that were either (1) not accurate or (2) represented an advance instead of an accrual, which was not considered in the statistical validation design. The inclusion of inaccurate survey responses in the statistical validation calculation prevented OCFO from producing a reliable point estimate and invalidated the statistical integrity of the process. These data inputs were used in the validation model to produce a point estimate to validate the estimate of fiscal year 2017 accrued grant liabilities of $2.2 billion. Also, by CPD's incorporating the flawed validation results into its fiscal year 2018 grant accrual estimation models, we believe there is an increased risk of misstatement of CPD's fiscal year 2018 grant accrual liability estimate. Further, if advances do exist, HUD's financial statements could be misstated due to their omission.

HUD Did Not Accurately Recognize Receivables Related to Sustained Audit Findings

HUD's third quarter accounts receivable balance included receivables from sustained audit findings totaling $159.8 million that were not always supported by a claim to cash, as required by Statements of Federal Financial Accounting Standards (SFFAS) 1.[17] While the sustained audit findings recommended repayment as an option, the management decisions did not state that HUD agreed and would require repayment. These findings and recommendations were made 4 to 7 years ago, there were no repayment agreements in place, and no collections had been made. Further, OCFO did not have an adequate allowance for loss methodology in place to estimate uncollectible amounts to reduce the gross amount of these receivables to its net realizable value. As a result, HUD's Accounts Receivable financial statement line item was potentially overstated

[16] Guidance provided to the grantees was limited to a frequently asked questions document, included with the survey letter, and followup phone calls to clarify abnormal information included in survey responses.

[17] SFFAS 1- Account for Selected Assets and Liabilities, paragraph 41: "A receivable should be recognized when a federal entity establishes a claim to cash or other assets against other entities, either based on legal provisions, such as a payment due date (e.g., taxes not received by the date they are due), or goods or services provided. If the exact amount is unknown, a reasonable estimate should be made."

by $159.8 million on its fiscal year 2017 and 2018 balance sheets. We attributed these conditions to the following deficiencies:

> _Lack of standard operating procedures_ – OCFO did not have standard operating procedures to ensure that sustained audit receivables were (1) accurately recorded or (2) periodically evaluated to assess collectability and determine an allowance for loss. As a result, it did not maintain source documentation for sustained audit receivables and relied solely on the information provided in the Office of Inspector General (OIG) audit reports[18] to support the receivable balance. While HUD's Debt Collection Handbook and Audits Management System Handbook provided some guidance on recording receivables related to sustained audit findings, they did not provide detailed procedures to properly account for and accurately value receivables that could arise from various types of audit reports in accordance with accounting standards. For example, they did not specify (1) that in addition to management a decision, HUD must have a claim to cash, such as a repayment agreement or demand letter, to record a receivable[19] and (2) how to evaluate sustained audit receivables periodically to assess collectability.
>
> _Followup on disallowed costs_ – OCFO reported that it kept these receivables on its books because the action officials did not contact it to indicate that they were delinquent. The Debt Collection Handbook states that action officials are responsible for monitoring disallowed costs. However, OCFO is ultimately responsible for HUD's financial reporting, and it did not have control activities to ensure that action officials fulfilled their responsibilities. Specifically, HUD's OCFO did not have a listing of all its action officials; therefore, OCFO could not efficiently and effectively perform inquiries and obtain information to determine whether the established receivables were valid.

HUD Did Not Recognize Prepayments for Funds Advanced to IHBG Grantees for Investment

During our audit of HUD's fiscal year 2015 financial statements,[20] we determined that HUD did not record an advance for the funds it disbursed to grantees for investment in advance of programmatic expenses in accordance with GAAP. Instead, HUD recorded an expense when disbursed. In HUD's September 30, 2018, financial statements, this practice understated HUD's assets by approximately $128.5 million. As this balance fluctuates, it could result in material misstatements.

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[18] HUD's Fort Worth Accounting Center reported that it did not know what source documentation was used to record these sustained audit receivables. The Fort Worth Accounting Center director stated that when he took over the accounts receivable function, he adjusted the balances to match the audit reports, since he had no support for the amounts that were previously booked.

[19] Ideally, the claim to cash occurs with a management decision; however, in practice, a claim to cash is not always established with a management decision. When OIG recommends repayment as an option to fulfill its recommendation, HUD does not have a claim to cash until it contacts the grantee and requires repayment or indicates that it will perform offsets.

[20] Audit Report 2016-FO-0003, Additional Details To Supplement Our Report on HUD's Fiscal Years 2015 and 2014 (Restated) Financial Statements, issued November 18, 2015

OCFO and the Office of Public Housing disagreed with this accounting treatment based on the fact that grantees were allowed to keep the interest earned on investments and that the Native American Housing Assistance and Self Determination Act of 1996 (NAHASDA) regulations allow for investing. We referred the disagreement to the Deputy Secretary, and on July 11, 2017, the Deputy Secretary concluded that since investment is an authorized program purpose, HUD's accounting treatment was correct and closed the recommendations. While we agree with all of these facts, they did not justify HUD's accounting treatment because they were irrelevant in evaluating these disbursements against GAAP.[21]

In response to our recommendation that OCFO perform an analysis using GAAP, OCFO used the accounting standards to determine that the investments were not HUD assets. Our evaluation determined that the analysis was fundamentally flawed because it argued that IHBG investments were not assets because they did not meet the following essential characteristics: (1) it embodies economic benefits or services that can be used in the future and (2) the government controls access to those economic benefits or services and can obtain or deny or regulate the access to those benefits or services.

We reviewed HUD's analysis and determined that (1) the investments did embody economic benefit or service because HUD receives its economic benefit or service when the investments are spent on an activity that fulfills HUD's mission, whereas funds held in investment accounts do not fulfill HUD's mission and (2) HUD controls access to the economic benefits through regulations over the investments, a depository agreement, and regulations on how the funds are spent once the investment period is over. These controls were put into place to ensure that HUD would receive its future economic benefit. While investing was permitted by NAHASDA, it was not a primary objective,[22] and while the money was held in investment accounts, it was not achieving HUD's mission. To achieve any of the primary objectives of the Act and contribute to HUD's mission, funds must be pulled from the investment account and spent on eligible activities. Therefore, the expense occurs when the grantee uses the money on an eligible activity and should be recognized as an advance before that event as described in SFFAS 1.

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21 SFFAS 1, "advances are cash outlays made by a Federal entity to its employees, contractors, grantees, or others to cover a part or all of the receipts' anticipated expenses or as advance payments for the good and services the entity acquires."

22 NAHASDA SEC. 201. NATIONAL OBJECTIVES AND ELIGIBLE FAMILIES. [25 U.S.C. (United States Code) 4131] (a) PRIMARY OBJECTIVE – The national objectives of this Act are-- (1) to assist and promote affordable housing activities to develop, maintain, and operate affordable housing in safe and healthy environments on Indian reservations and in other Indian areas for occupancy by low-income Indian families; (2) to ensure better access to private mortgage markets for Indian tribes and their members and to promote self-sufficiency of Indian tribes and their members; (3) to coordinate activities to provide housing for Indian tribes and their members with Federal, State, and local activities to further economic and community development for Indian tribes and their members; (4) to plan for and integrate infrastructure resources for Indian tribes with housing development for tribes; and (5) to promote the development of private capital markets in Indian country and to allow such markets to operate and grow, thereby benefiting Indian communities."

In fiscal year 2018, we reopened all recommendations related to this issue. We will continue to review and report this issue as a departure from GAAP until a thorough analysis is completed of the accounting treatment using Federal GAAP and other accounting standards and regulations applicable to HUD's financial reporting framework.

HUD Did Not Use Complete and Accurate Data To Estimate Its PIH Prepayment Balance

Before fiscal year 2018, PIH used restricted net position (RNP) reports to determine the PIH prepayment related to the Housing Choice Voucher Program (HCVP) presented on HUD's balance sheet. In fiscal year 2017, we found that the lack of OCFO involvement and the manual nature of this accounting estimate resulted in haphazard accounting and untimely and inaccurate balances. In response to our recommendations, OCFO developed a new methodology to estimate PIH's prepayment related to the HCVP. While PIH and OCFO have worked together, we noted weaknesses in PIH's communication and OCFO's validation of important information impacting the reliability and accuracy of the estimate. Specifically, we found the following:

> *<u>PIH provided incorrect and incomplete information to OCFO</u>* – First, PIH provided OCFO with an outdated version of the document it previously used to determine which Moving to Work Demonstration (MTW) Voucher Management System (VMS) expense fields to include. The outdated version did not include significant MTW expenses that should be considered in the PIH prepayment estimate. Second, PIH did not provide complete information to OCFO regarding the inclusion of MTW administrative fee expenses. Under PIH's previous methodology, MTW administrative fee expenses were included in the PIH prepayment estimate only if the public housing agency's (PHA) administrative fee revenue did not cover its administrative expenses. Third, PIH did not inform OCFO that there were updates to the December 31, 2016, beginning balance based on final Financial Management Council (FMC) and Quality Assurance Division (QAD) reviews.
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> *<u>OCFO did not perform adequate validation procedures</u>* – OCFO did not perform a validation against the data previously used by PIH. This validation would have ensured that PIH provided the correct information on MTW VMS expense fields and that OCFO included the correct CAM 1 codes[23] in its estimate.
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> *<u>Standard operating procedures were developed after the estimate was prepared</u>* – OCFO did not finalize its PIH prepayment procedures until after the estimate was calculated and HUD's third quarter statements were prepared.

As a result, OCFO used incomplete and inaccurate data to (1) estimate the third quarter PIH Prepayment financial statement line item presented on HUD's balance sheet and (2) recalculate the estimate used for the PIH prepayment balance as of September 30, 2017. Specifically, (1)

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[23] CAM 1 is an accounting flex field. The accounting flex field represents the accounting strip or line of accounting and must be present on every transaction in Oracle Federal Financials. Segments include fund, budget fiscal year, USSGL, budget objects class, internal org, cost pool, Cam 1, category B, program, cohort, Cam 2, and Cam 3. HUD is using CAM 1 codes to differentiate between its various HUD programs.

significant MTW expenses were missing, (2) not all CAM 1 codes were included, (3) the beginning balance did not include the results of FMC and QAD reviews, and (4) the entire MTW administrative expense was included regardless of the administrative revenue received. After we inquired, OCFO determined that its third quarter estimate incorrectly excluded significant MTW expenses. Upon updating its procedures to include these expenses, it was determined that the third quarter estimate of $222 million should be $116 million. However, this amount did not include corrections for the other inaccuracies discussed above.

Due to the multiple deficiencies and the various impacts on the estimate, we cannot quantify the total potential misstatement. However, the deficiencies noted above could cause significant misstatements. In addition, the prepayment balance on the yearend financial statements was at risk of being materially misstated. Additionally, as disbursements and expenses fluctuate, these deficiencies could have greater impacts on future PIH prepayment estimate calculations.

HUD Did Not Recognize All Financial Events Resulting From PIH's Cash Management Process

As described in the section above, there were weaknesses in estimating the PIH Prepayment line item on HUD's financial statements. The PIH Prepayment line item requires estimation because PIH does not have a system capable of (1) determining PHA expenses in real time or (2) automatically calculating the difference between HUD's disbursements and PHA expenses at the PHA level. This issue not only impacts the PIH prepayment calculation, but also inhibits HUD from accurately calculating and recording other transactions that result from PIH's cash management process. For example, as part of the cash management process, PIH performs cash reconciliations to identify overpayments and underpayments owed to and from PHAs. However, cash reconciliations cannot be completed in a timeframe to allow for timely financial reporting. By the time the reconciliations are completed to identify the overpayments and underpayments (receivables and payables), they are likely not representative of the current status of the receivables or payables.

In the absence of a system, OCFO has developed procedures to estimate the PIH prepayment; however, it has not done the same for the receivables and payables that result from cash reconciliations. We attributed this condition to the fact that OCFO has not completed a review of the entire cash management process to (1) identify all financial events resulting from cash management activity to be recognized in accordance with GAAP and (2) establish procedures for accounting for those financial events properly and in a timely manner in accordance with GAAP. As a result, when PIH determined that it had overpaid PHAs $120.7 million or underpaid PHAs $199.7 million through its December 31, 2017, cash reconciliations, accounts receivables and payables were not recorded to recognize HUD's claim to cash and liability. This condition understated both line items and overstated the PIH prepayment by the amount of the receivable. The total amount of these misstatements in HUD's fiscal year 2018 financial statements cannot be quantified because as discussed above, receivables and payables are unknown until several months after the point of recognition.

In addition, although OCFO recorded an estimate for the PIH prepayment, financial transactions were not recognized at the transaction level. When HUD disburses funds to PHAs or PHAs spend funds provided by HUD, the PIH prepayment balance is impacted. However, these changes were not recognized as they occurred and at the transaction level in HUD's general ledger. Instead, OCFO recorded manual journal entries quarterly to adjust the balance to agree with its estimate.

In our audit of HUD's fiscal year 2013 consolidated financial statements, we recommended that PIH automate its cash reconciliation process;[24] however, this recommendation still does not have a management decision. In fiscal year 2018, PIH reported that it was waiting for the release of funding from OCPO to procure a contract to automate the cash management process. We inquired with PIH about entering a management decision since it appeared that it was making progress on addressing this recommendation. However, as of September 30, 2018, PIH had provided no management decision.

Conclusion

In fiscal year 2018, HUD did not properly account for all of its assets, liabilities, or budgetary resources in accordance with Federal GAAP. This condition occurred because HUD did not have adequate internal controls or systems to ensure accurate accounting. As a result, several line items in HUD's financial statements were misstated, unsupported, or at risk of misstatement. Specifically, HUD's (1) use of FIFO to account for fiscal year 2014 and prior CPD grants and systemic weaknesses within DRGR led to material misstatements of HUD's unobligated balances and related line items; (2) $335.4 million in HUD's capitalized property, plant, and equipment were unsupported and could not be audited; (3) accrued grant liabilities and PIH prepayment estimates were at risk of misstatement; (4) receivables from sustained audit findings were potentially overstated by $159.8 million; and (5) IHBG prepayments and cash management accounts receivables and payables were not recognized.

Recommendations

Several prior-year recommendations regarding the CPD accrued grant liabilities; accounting for cash management activity in the HCVP; IHBG advances; and property, plant, and equipment portions of this finding remained open and can be referred to in the Followup on Prior Audits section of this report. We have the following new recommendations.

We recommend that the Chief Financial Officer

2A. Evaluate the impact of the DRGR weaknesses identified in audit memorandum 2018-FW-0802 during the improper payment risk assessment process.

2B. Evaluate the impact of the improper accounting for grant funds issued under the Disaster Relief Appropriations Act, 2013, identified in audit memorandum 2018-FW-0802 and perform an adjustment or restatement of the impact if deemed significant.

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[24] Audit Report 2014-FO-0003, Additional Details To Supplement Our Report on HUD's Fiscal Years 2013 and 2012 (Restated) Financial Statements, issued December 16, 2013

2C. Work with CPD on remediation plans to address application control weaknesses within DRGR identified by audit memorandum 2018-FW-0802 that have contributed to continuing FFMIA noncompliance.

2D. Require the grantees to submit supporting documentation with their survey responses to substantiate the amounts certified in support of OCFO's validation of grant accrual estimates.

2E. Provide periodic training to grantees to assist them with understanding and completing the information requested in the survey letter to validate HUD's grant accrual estimates.

2F. Research the survey responses received as part of OCFO's validation of grant accrual estimates that resulted in a positive cash on hand to determine whether a cash advance exists. If so, OCFO should coordinate with CPD to (1) determine whether the grantees have proper documentation and approvals allowing for cash advances and (2) develop and implement procedures to estimate and account for cash advances for financial reporting purposes.

2G. Develop and implement standard operating procedures for recording and periodically evaluating sustained audit receivables to ensure that (1) all receivables are supported by a claim to cash and (2) an allowance for loss is recorded that reasonably estimates uncollectible amounts to reduce the gross amount of receivables to its net realizable value.

2H. Develop and implement procedures that require action officials to certify the validity of accounts receivables periodically, at least quarterly. OCFO should use this information to assess the reasonableness of the allowance for loss estimate.

2I. Work with action officials to determine the validity of all receivables from OIG sustained audit findings, determine whether restatement is necessary, and adjust HUD's current and prior-year accounts receivable balances accordingly, ensuring that all writeoffs are reported to the Treasury.

2J. Perform a validation, comparing the data used in OCFO's PIH prepayment estimate calculation to the data used by PIH in its RNP reports to ensure that all CAM 1 codes and VMS fields are appropriately included. If it is determined that CAM 1 codes or VMS codes are missing or not properly included, OCFO should update the standard operating procedure and all estimates made to ensure that they are included.

2K. Design and implement a procedure that ensures periodic communication between OCFO and PIH regarding all events that impact the PIH prepayment estimate.

2L. Review FMC's final December 31, 2016, balances and update the PIH prepayment beginning balance accordingly.

We recommend that the General Deputy Assistant Secretary for Public and Indian Housing

2M. Design and implement a policy or procedure that ensures the accuracy of all information provided to HUD OCFO related to the PIH prepayment estimation methodology.

Finding 3: HUD's Financial Management System Weaknesses Continued

HUD's financial system weaknesses remained a material weakness in fiscal year 2018 due to the continued impact of a multitude of financial reporting deficiencies and limitations. While HUD took steps to address financial management system weaknesses during fiscal year 2018, significant challenges remained. Many of the material weaknesses discussed in this audit report share the same underlying cause, shortcomings in HUD's financial management systems. Specifically, we noted (1) issues remaining from the transition of key financial management functions to an FSSP, (2) existing financial management systems that lacked key functionality, and (3) HUD's not having financial systems in place to meet financial management needs. HUD's efforts to modernize its financial management systems have been hindered by weaknesses in implementing key IT management practices.[25] HUD's inability to modernize its legacy financial systems has resulted in a continued reliance on legacy financial systems with various limitations. Program offices have compensated for system limitations by using less reliable manual processes to meet financial management needs. These system issues and limitations inhibited HUD's ability to produce reliable, useful, and timely financial information and contributed to a multitude of financial reporting errors and HUD's inability to obtain an unqualified opinion on its consolidated financial statements.

HUD Had Longstanding IT Project Planning and Management Weaknesses Related to Financial Systems

While HUD has long recognized the need to modernize its outdated legacy financial management systems, efforts have fallen short due to persistent weaknesses in HUD's IT project planning and management. Despite spending approximately $370 million in a succession of financial system modernization initiatives since 1991, HUD continues to rely on legacy financial systems that were developed 15 to 30 years ago with various limitations that hinder HUD's ability to achieve its mission. HUD's inability to retire or decommission legacy financial systems due to IT project planning and management weaknesses has required it to allocate significant IT funds on the expensive operation and maintenance of legacy systems. Therefore, HUD has very limited resources to fund any new IT system developments. These circumstances have hindered HUD's ability to improve its data quality and ensure reliable and accurate financial reporting.

In fiscal year 2017, HUD started using the GrantSolutions[26] application as part of a departmental grant modernization initiative. However, ensuring that the data were included in HUD's general

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25 U.S. Government Accountability Office (GAO), GAO-16-656, July 2016, Financial Management Systems: HUD Needs to Address Management and Governance Issues That Jeopardize its Modernization Efforts; http://www.gao.gov/assets/680/678727.pdf

26 GrantSolutions is a grant management system offered as a shared service by the Grants Center of Excellence at the U.S. Department of Health and Human Services. HUD has incorporated the Grants Management Module (GMM) of GrantSolutions to make awards for its program offices. The GMM generates the required funding documents, including the notice of award (NOA), which replaces the use of HUD forms HUD-1044 for grant agreements. While considering funds control, the NOA serves as the legal point of obligation (obligating document) for program offices.

ledger required manual processes and reliance on HUD's legacy systems, HUD lacked formal policies and procedures related to the use of the system, and we noted control weaknesses related to segregation of duties within the system. Refer to Finding 6 for additional details.

While steps have been taken in an attempt to modernize HUD's grants process across the Department, a substantial majority of HUD's transactions are still processed through HUD's legacy systems that are no longer supported by vendors, increasing the risk of failure and posing substantial operational risk to the Department.

Significant Issues Remained From HUD's Transition to ARC and Oracle Federal Financials

In prior years, we have reported on issues HUD experienced following the transition of key financial management functions to an FSSP with release 3 of the New Core Project on October 1, 2015.[27] As of September 30, 2018, transaction processing using the New Core Financial Management Solution had improved, but challenges and weaknesses remained. For example, ARC was still correcting accounting flex fields (AFF)[28] that were incorrect or missing converted data. In fiscal year 2018, ARC adjusted approximately $90 billion in transactional data to correct AFFs.

HUD's Financial Systems Lacked Key Functionality

Several of HUD's financial systems used to support significant balances on the financial statements lacked key functionality. This deficiency prevented HUD from relying on the data output provided and reporting key financial statement balances in accordance with GAAP.

Ginnie Mae Systems Were Unable To Track Loan-Level Activity in Defaulted Issuer Portfolio

Ginnie Mae did not have systems to adequately record and account for the loan accounting and processing of activity in its defaulted issuers' portfolio and remained unable to support key financial statement line items related to its nonpooled loans portfolio acquired from defaulted issuers. Ginnie Mae's challenges come from its lack of a financial system (or systems) capable of recording loan-level transaction details in compliance with GAAP accounting requirements. Material weaknesses related to Ginnie Mae's nonpooled loans portfolio, approximately $3 billion and $3.6 billion, as of September 30, 2018, and September 30, 2017, remained unresolved as of September 30, 2018.

Additionally, Ginnie Mae did not have an accounting system to account for and track servicing costs at a loan level. As a result, it was reliant on third-party master subservicers' cash-basis data that did not account for GAAP-basis reimbursable costs. We concluded that Ginnie Mae failed to adequately establish and maintain accounting systems to manage and control the loan

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[27] New Core was HUD's financial system modernization program, initiated in 2013, that involved migrating financial management capabilities to an FSSP with expected benefits, including reduced legacy system costs, improved data, and remediated audit deficiencies.

[28] The accounting flex field represents the accounting strip or line of accounting and must be present on every transaction in Oracle Federal Financials. Segments include fund, budget fiscal year, USSGL, budget objects class, internal org, cost pool, Cam 1, category B, program, cohort, Cam 2, and Cam 3.

accounting and processing of the activities related to its defaulted issuers' portfolios. Refer to the relevant material weaknesses and associated recommendations for additional details.[29]

<u>DRGR Weaknesses Did Not Adequately Address Disaster Grant Program Risks</u>

A fiscal year 2018 OIG program audit noted significant weaknesses within the Community Development Block Grant Disaster Recovery program and CPD's DRGR system related to the obligation and disbursement of funds from the Disaster Relief Appropriations Act, 2013.[30] Specifically, OIG identified potential ADA violations and transactions that did not comply with GAAP. Due to weaknesses in the DRGR system, grantees were able to spend more than obligated in grant rounds and record expenses both before and after grant rounds were obligated. Additionally, DRGR system weaknesses did not enable CPD personnel to identify potential ADA violations or GAAP noncompliance. These weaknesses prevented HUD from ensuring the accuracy and reliability of its financial reporting on the status of budgetary resources related to CPD disaster grants from the Disaster Relief Appropriations Act, 2013. Refer to finding 2 for more detail.

<u>IDIS Remained Unable To Properly Account for Formula Grant Transactions</u>

While CPD completed IDIS system configuration updates in early fiscal year 2018 to address the inappropriate FIFO method of accounting for grant disbursements, management's decision to implement appropriate grant accounting for only fiscal year 2015 and forward grants continued to impede HUD's ability to resolve material weaknesses and comply with FFMIA. The material weakness and FFMIA noncompliance related to CPD's formula grant accounting will not be completely addressed until the amounts subject to FIFO become immaterial. The amount of obligations susceptible to the FIFO method was approximately $1.1 billion and $1.5 billion as of September 30, 2018, and September 30, 2017, respectively.[31]

<u>Property, Plant, and Equipment Data Remained Unreliable</u>

Despite taking steps toward addressing longstanding property management system weaknesses during fiscal year 2018, unresolved control deficiencies continued to impede HUD's ability to support key property, plant, and equipment balances, including internal use software and leasehold improvements. We were unable to audit the balances reported on HUD's financial statements related to general property, plant, and equipment due to ineffective internal controls and an unsupported subsidiary ledger, causing OCFO to deem this area out of scope for the current-year audit. While HUD used the Federal Asset Management Enterprise System (FAMES)[32] as its asset management system, addressing the longstanding departmental need for a working asset management system, FAMES data remained unreliable. Additionally, HUD inconsistently recorded key data elements during the course of a fiscal year 2017 physical inventory, resulting in the continued unreliability of physical asset balances in FAMES. OCFO, OCIO, and OA must work to implement corrective actions and effective controls to adequately

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[29] Audit Report 2019-FO-0001, Audit of the Government National Mortgage Association's Financial Statements for Fiscal Years 2018 and 2017 (Restated), issued November 13, 2018

[30] Audit Memorandum No. 2018-FW-0802, Interim Report – Potential Antideficiency Act and Generally Accepted Accounting Principle Violations Occurred With Disaster Relief Appropriation Act, 2013, Funds, May 15, 2018

[31] Refer to finding 2 of this report.

[32] FAMES is HUD's property inventory system owned by OA.

support property, plant, and equipment balances that remained unauditable as of September 30, 2018.

HUD Did Not Have Financial Systems in Place To Meet Financial Management Needs

In addition to weaknesses and limitations associated with HUD's existing financial systems, HUD did not have systems in place to meet other financial management needs.

HUD Lacked an Effective Cost Accounting System

In fiscal year 2006, the U.S. Government Accountability Office (GAO) first reported on a lack of managerial cost accounting functionality within HUD's financial management system.[33] Further, GAO noted the continuing effect of inadequate cost accounting and allocation practices in a fiscal year 2017 report, noting that HUD's cost estimates for IT investments exhibited significant weaknesses and were generally unreliable.[34] As of fiscal year 2018, HUD continued to lack adequate cost allocation and accounting systems and processes to accurately report on the cost of programs, assist in managing daily operations, and effectively estimate projected costs. Specifically, HUD did not consistently allocate administrative and IT costs to all program offices and components, resulting in noncompliance with Federal accounting standards and other requirements. Additionally, a lack of policies and procedures between OCFO and FHA and the exclusion of Ginnie Mae data from the process have resulted in incomplete and inaccurate cost allocation.[35] As a result, HUD's cost misallocations required 2017 financial statement restatements of $174 million to address inappropriately allocated cost allocation practices. HUD's lack of adequate cost accounting and cost allocation system functionality continued to hinder HUD's ability to produce reliable performance information and impeded HUD's ability to provide accurate financial reporting and estimates.

PIH Cash Management Activities Were Not Fully Accounted For

As described in finding 2, PIH did not have a system with the capability of (1) determining PHA expenses in real time or (2) automatically calculating the difference between HUD's disbursements and PHA expenses at the PHA level (transaction level). Without a system, PIH used complex spreadsheets that included extracted data from multiple systems and manual tracking logs to determine the amount each of its 2,200 PHAs were holding and the amount that it should offset to follow cash management requirements. The use of multiple Excel files, instead of a system, increased the risk of human error due to a lack of access controls, version controls, and traditional data-processing controls normally embedded in applications. Further, without a system, (1) the PIH Prepayment line item must be estimated and cannot be accounted for at the transaction level and (2) other transactions that result from PIH's cash management process, such as receivables and payables, cannot be accurately determined and recorded.

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[33] GAO-06-1002R, Managerial Cost Accounting Practices, dated September 21, 2006
[34] GAO-17-218, HUD Needs to Address Significant Weaknesses in Its Cost Estimating Practices, http://www.gao.gov/assets/690/682537.pdf
[35] Refer to finding 2 of this report.

HUD Lacked Systems To Properly Account for Section 108 and 184 Loan Guarantee Programs
A lack of systems to account for the Section 108 and 184 loan guarantee programs in the past contributed to HUD's inability to support related general ledger balances. Specifically, during fiscal year 2018, HUD had to make adjusting entries to its memorandum accounts to correct unsupported balances. HUD now uses Oracle as its subsidiary ledger for these programs; however, there is no interface between Oracle and the systems used to track daily loan guarantee activity. As a result, this activity must be manually loaded into Oracle. In fiscal year 2018, ARC used approximately 1,135 journal vouchers totaling $3.7 billion to account for HUD's loan guarantee activity.

FHA Did Not Have a System in Place To Account for Its $1.5 Billion Direct Loan Portfolio
FHA did not have a system in place to generate reliable and detailed loan-level accounting reports for its $1.5 billion portfolio of Federal Financing Bank (FFB) direct loans and related borrowings. FHA had to use data from Treasury and FFB reports to manually create journal entries to record loan receivables instead of recording the transactions when events triggered accounting entries. FHA's accounting for the FFB direct loans and related borrowings was susceptible to errors due to the labor-intensive manual process, reliance on summarized reports from Treasury and FFB, and undocumented policies and procedures. FHA risked not being able to record and report loan-level transactions accurately, completely, and in a timely manner as well as not being able to identify material misstatements in a timely manner due to the increased probability of errors and delays inherent in the manual accounting processes that had been informally undertaken.

Conclusion
Complete and reliable financial information is critical to HUD's ability to accurately report on the results of its operations to internal and external stakeholders. During fiscal year 2018, system limitations and weaknesses continued to contribute to the possibility that a material misstatement of HUD's financial statements would not be prevented or detected and corrected in a timely manner. Until these weaknesses are fully remedied, HUD's ability to produce reliable, useful, and timely financial information needed for accountability, performance reporting, and decision making will remain a departmental material weakness.

Recommendations
Prior-year recommendations regarding this finding remained open and can be referred to in the Followup on Prior Audits section of this report. Additional recommendations regarding HUD's financial management systems have also been reported under other findings in this and prior-year audit reports. Therefore, we have no new recommendations in this report.

Significant Deficiencies

Finding 4: HUD's Financial Management Governance Had Progressed, but Weaknesses Remained

During fiscal year 2018, HUD experienced progress with its financial management governance; however, several areas remained unaddressed. As of September 30, 2018, (1) HUD's financial management leadership structure was strengthened by key positions being filled; however, key personnel roles remained vacant in OCFO; (2) OCFO continued to experience problems with information and communication necessary to allow for accurate financial reporting; (3) development of policies and procedures for significant business practices had progressed, but HUD continued to lack mature financial management governance practices; (4) HUD did not have reliable financial information for reporting; and (5) weaknesses in HUD's financial management systems continued. Weaknesses in program and component internal controls, which impacted financial reporting, were able to develop in part due to a lack of established financial management governance processes. These unaddressed financial management weaknesses significantly contributed to the (1) material weaknesses and significant deficiencies in internal controls over financial reporting, (2) instances of noncompliance with laws and regulations, and (3) consecutive years of restating prior-year financial statement balances to correct errors. While financial management leadership had begun setting the preliminary direction and priorities to ensure proper oversight and implementation of robust financial management practices, HUD continued to experience challenges with resolving these deficiencies.

Fulfillment of Key OCFO Positions Improved HUD's Establishment of Effective Internal Control

HUD has filled vacancies in key OCFO positions that previously had significant financial and operational risks related to financial reporting. For example, the presidential appointment of HUD's CFO was confirmed by Congress in the first quarter of 2018. Additionally, key positions, including the Deputy CFO, the Assistant CFO for Budget, and the Director of the Financial Reporting Division, were filled during the fiscal year, which improved the operational effectiveness of OCFO. In prior years, we reported that the impact of these high-level personnel changes, coupled with the absence of a confirmed CFO for multiple years, impeded OCFO's ability to effect change in its internal control framework for financial reporting and budgetary accounting. The new CFO improved the internal structure of OCFO, strengthening and aligning the competences and resulting in an improved mission- and process-focused office. Since these key positions have been filled, the responsibilities among assistant CFOs have been clearly defined, performed, and monitored, allowing for material weaknesses and other deficiencies in financial reporting and internal funds control to improve or be substantially addressed.

Despite improvements in filling key positions, vacancies in some critical financial management positions continued to exist, including the Director of the Risk Management Division and the Director of the Financial Systems Maintenance Division. Further, shortly after the end of fiscal year 2018, the Director of the Funds Control Assurance Division departed. Due to the recurring trends of vacancies in many key positions, OCFO needs to continue to work diligently in identifying skilled, competent personnel to fill these roles in a timely manner to ensure continuity and that the mission and objectives of the CFO are achieved. Otherwise, HUD's financial integrity will continue to be at substantial risk of not complying with Federal laws, regulations, and accounting standards.

Weaknesses in Communication and Sharing of Information Continued

We have reported on weaknesses in information and communication within OCFO and HUD since fiscal year 2012. Although improvements have been made within OCFO and among HUD's departments and program offices, maintaining effective information and communication has been a consistent departmental challenge that continued during fiscal year 2018. We noted continued communication challenges in OCFO in the areas of financial reporting and the sharing of information and communication with HUD program offices.

As discussed in finding 1, HUD's internal control system did not have effective controls to reasonably ensure that it gathered and accurately included all necessary information from its component entities, program offices, and OGC into its consolidated financial statements. While there is regular communication and a certification process between HUD and its component entities (Ginnie Mae and FHA), there are still shortcomings in HUD's processes for gathering and validating information from all applicable parties and properly presenting it in the financial statements. Due to these deficiencies, (1) HUD's third quarter fiscal year 2018 financial statements and notes were misstated and missing required information, (2) HUD's fiscal year 2017 financial statements contained errors and required restatement, and (3) HUD's fiscal year 2018 financial statements are at risk of material misstatement.

Further, component and program office accounting policies and procedures were, at times, developed without adequate OCFO input due to broad delegations of key financial management functions to component and program office personnel. We attributed the findings reported in finding 2 regarding PIH cash management activity and finding 8, noncompliance with the Debt Collection Improvement Act (DCIA), to continued weak oversight and collaboration between OCFO and program offices.[36] These deficiencies occurred in prior years and continued during fiscal year 2018.

- *PIH cash management.* In fiscal year 2017, we found that the lack of OCFO involvement and the manual nature of the PIH prepayment estimate resulted in haphazard accounting and untimely and inaccurate balances. In response, OCFO developed a new methodology to estimate PIH's prepayment related to the HCVP. While PIH and OCFO have worked together, we noted weaknesses in PIH's communication and OCFO's validation of important information impacting the reliability and accuracy of the estimate. Further, OCFO had not completed a review of the entire cash management process to identify all financial events resulting from cash management activity to be recognized in accordance with GAAP. This weakness resulted in misstatements on HUD's interim and final fiscal year 2018 balance sheets and noncompliance with GAAP and FFMIA.

[36] Refer to finding 2 of this report.

- *Noncompliance with DCIA*. In audit report 2018-FO-004[37] and audit report 2017-LA-0005,[38] we reported that HUD's OCFO needed to strengthen its controls to ensure compliance with DCIA. In fiscal year 2018, we noted little improvement in this area and learned that OCFO was missing foundational information needed to reasonably ensure that all of HUD's debts comply with DCIA. Refer to finding 8 for additional details.

Organizational Assessments Found Weaknesses Within HUD's Financial Management and Internal Controls

Over the last few years, organizational assessments and reviews have been conducted by HUD, GAO,[39] and other subject-matter experts[40] that have largely echoed our reporting on HUD's governance weaknesses and the negative impact those weaknesses have had on internal controls and the achievement of departmental objectives.

HUD senior management formed the FMC[41] to improve the Executive Operations Council established in fiscal year 2017. As reported in the prior year, the FMC failed to meet in the last quarter of fiscal year 2017 due to leadership changes. However in fiscal year 2018, HUD demonstrated improvements in its commitment to addressing internal control risks by routinely meeting monthly, beginning in the second quarter of 2018; completing an updated enterprise risk management (ERM) risk profile; and executing OMB Circular A-123, Appendix A, Internal Control Over Reporting, reviews for (1) data completeness, (2) funds control compliance, (3) complementary controls, (4) validation of financial statement notes, and (5) OMB Circular A-136 reporting requirements. The results of the reviews indicated that HUD's management must improve internal controls over financial reporting through its governance structure. The data completeness assessment noted that of 30 key controls over financial reporting (12) and funds control (18), 20 controls were either not documented or not being performed, resulting in a 67 percent error rate. Based on the testing results, current key internal controls over the completeness of data recorded in Oracle were not designed and operating effectively.

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[37] Audit Report 2018-FO-0004, Additional Details To Supplement Our Fiscal Years 2017 and 2016 (Restated) U.S Department of Housing and Urban Development Financial Statement Audit

[38] Audit Report 2017-LA-0005, HUD Did Not Always Follow Applicable Requirements When Forgiving Debts and Terminating Debt Collections

[39] GAO-16-656, FINANCIAL MANAGEMENT SYSTEMS, HUD Needs to Address Management and Governance Weaknesses That Jeopardize Its Modernization Efforts, https://www.gao.gov/assets/680/678727.pdf

[40] Department of Housing and Urban Development, Office of Chief Financial Officer, Organizational Assessment, March 19, 2015, http://napawash.org/images/reports/2015/HUD_OCFO_Study_Final_Report.pdf. The National Academy of Public Administration made three high-level recommendations, concluding that HUD should (1) improve financial management oversight and governance, (2) address concerns associated with the transition to the FSSP, and (3) strengthen the finance workforce. This review supported the longstanding OIG recommendation that HUD establish a management council to enhance financial governance.

[41] The FMC serves the purposes of the Senior Management Council as set forth in OMB Circular A-123, Management's Responsibility for Enterprise Risk Management and Internal Control. The FMC provides oversight and guidance for HUD financial activities, financial-related audits, and the management control program.

In the prior year, we reported that HUD had not designed or implemented effective complementary customer agency controls to leverage FSSP controls.[42] We determined that HUD resolved the financial reporting controls of reviewing key account reconciliations and validating FSSP-prepared financial reports during fiscal year 2018. In our review of additional complementary controls tested in HUD's OMB Circular A-123, appendix A, assessment, we found that financial reporting complementary controls relating to budgetary accounting, manual journal entries, and salaries and expenses funding were either not designed, documented, or operating effectively. Specifically, of four controls over financial reporting and 18 funds controls tested, 10 controls were either not documented or designed correctly or not being performed as designed, which posed the potential risk of budget information not being recorded in the general ledger accurately and in a timely manner, including apportionments in Standard Forms 132 and allotments in form HUD-158. When assessing the progress of implementing complementary controls for all HUD program operations using the FSSP, we noted that the programs established 50 controls (47 for FSSP and 3 for IT) in 2018. The implementation of the controls was supported by a documented HUD management-approved control description, with the exception of two financial reporting controls.

While the internal control assessments described above provide essential information to management to improve governance, the effectiveness of HUD's FMC will be limited if HUD senior management does not make the FMC and its responsibilities a priority and does not take timely action to address the internal control weaknesses noted in its OMB Circular A-123 reviews and other organizational assessments. These results from the A-123 assessments, coupled with unremediated material weaknesses, prompted OCFO to provide a statement of no assurance regarding the effectiveness of internal controls over financial reporting, which fed into HUD's 2018 overall statement of assurance reported in its AFR. The assessment portrays challenges facing HUD as it attempts to address outstanding material weaknesses, significant deficiencies, and instance of noncompliance with laws and regulations.

HUD's Efforts To Address Internal Control Deficiencies Had Progressed

In prior years, we have reported that HUD was not addressing internal control deficiencies in a timely manner in accordance with internal control requirements and OMB Circular A-50, Audit Followup. The timely remediation of identified control deficiencies is a key element of the monitoring component outlined in GAO's Green Book, Standards for Internal Control in the Federal Government. While a significant number of prior-year recommendations remain open, we noted improvements in this area during fiscal year 2018.

In quarter two of 2018, HUD began the OCFO Finance Transformation initiative for improving people, processes, and technology agencywide. The initiative highlights the following areas of weaknesses at HUD: (1) governance and controls, (2) shared services and technology, (3) financial reporting, (4) accounting operations, and (5) grants management. OCFO identified

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[42] The Green Book provides internal control considerations for service organizations including FSSPs. Service organization internal control considerations include establishing complementary customer agency controls, or "user organization controls," at the agency receiving services.

operational and functional challenges in each of these areas and has offered corrective action activities to implement going forward, including those relating to prior-year financial statement audit recommendations. While identifying weaknesses and offering corrective actions to mitigate them is a positive step, we concluded that the initiative is in the preliminary stages.

As part of this enterprisewide initiative, OCFO developed and is in the process of executing several remediation plans to address multiple financial statement audit material weaknesses and associated recommendations. The corrective actions associated with these plans are ongoing, and some will not be fully implemented for a number of years. However, this is another indication that efforts to address internal control deficiencies have improved, corrective actions are underway, and addressing internal control deficiencies in a timely manner has become an agency priority.

As of October 30, 2018, 56 of 80, or 70 percent, of OIG recommendations from prior-year financial statement audit reports were past the agreed-upon dates for final action. Further, we noted that as of October 30, 2018, management had not established action plans for 12 additional recommendations, which was a decrease from 20 recommendations without action plans as of October 13, 2017. While the number of outstanding recommendations has not significantly decreased since the prior year, it will take time before the execution of multiple strategic plans and implementation of HUD's finance transformation initiative will have a substantial impact on the number of outstanding recommendations.

HUD's Implementation of a Financial Policy Framework Had Progressed

During fiscal years 2016 and 2017, we identified weaknesses resulting from HUD's pervasive lack of policies and procedures. Further, as noted in the prior year, in fiscal year 2016, GAO noted that weaknesses in HUD's governance across various management functions may reduce the agency's ability to effectively and efficiently accomplish its mission, including outdated or incomplete policies and procedures. With the direction of the CFO and HUD management, there has been an initiative to implement corrective actions to address this issue in 2018.

In prior years, we recommended that HUD improve the continuity of accounting policies and procedures in a changing environment and that internal policies and procedures be centrally located and easily accessible to all staff. In fiscal year 2018, HUD began to incorporate key elements of internal control into its financial management operations. Specifically, HUD implemented control activities through the implementation of various policies and procedures. Notably, the OCFO Policy Development Framework, 2018.1, established a policy framework, which requires the periodic review of policies and procedures to ensure that HUD's documentation accurately reflects current business processes. Further, the CFO Handbook 1980.1 for accounting policies has had several revisions for key financial reporting and internal processes, including subledger reconciliations; consolidation of financial statements; property, plant, and equipment; and administration of funds. Standard operating procedures for HUD's financial statement preparation and reporting were also developed and implemented during fiscal year 2018. The development of these policies and procedures has allowed HUD to begin resolving internal control weaknesses to which a lack of policies and procedures was a contributing factor.

As of September 30, 2018, we concluded that HUD has made efforts to address GAO's and our recommendations for enhanced policies and procedures for financial reporting and internal control. It is important for OCFO and HUD to sustain these efforts to ensure that internal control weaknesses do not arise again.

HUD Had Not Assigned Risk Mitigation Responsibilities for Enterprise Risk Management

HUD continues to be in the process of integrating ERM into the internal control framework under the leadership of the Chief Risk Officer and OCFO. They are responsible for ensuring HUD's compliance with ERM requirements, including conducting annual risk profiles and mitigation of risk identified in the annual reviews. Through HUD's efforts to implement ERM, its risk profile. containing 151[43] risks across 14 program areas, was reviewed and updated in fiscal year 2018. Of the 151 risks identified, 51 were categorized as Level I Risk Category – Reporting, having a direct impact to financial reporting across 10[44] program offices. OCFO is primarily responsible for 16 risks associated with financial, operational, and compliance-based risks.

According to HUD's timeline, mitigation strategies were expected to be completed for all risks from June 19 to July 9, 2018; however, a review of HUD's ERM risk portfolio as of August 21, 2018, found that 80 of the 151 active risks did not have proposed risk responses.[45] As stated above, OCFO is primarily responsible for reporting, operational, and compliance-based risks. Of these 16 risks, only 10 have been assigned a risk owner and a risk response. As a result of the lack of mitigation strategies for its identified enterprise risks, HUD cannot provide a complete accountability report on its identified material weaknesses and corrective risk response actions as required by OMB Circular A-123, Management's Responsibility for Enterprise Risk Management, and risks will continue to affect accurate financial reporting and the potential for fraud to exist. Mitigation strategies, including enhancing internal controls for reporting, operations, and compliance, are needed to effectively manage HUD's risk and improve its accountability and effectiveness across its program offices. HUD management needs to properly assign risk owners to provide responses for the acceptance, mitigation, and elimination of governance, reporting, monitoring, culture, and technology risks.

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43 The risk profile contained 169 risks. This amount is comprised of 151 active risks, 15 downgraded risks, 2 retired risks, and 1 deleted risk. These risk actions are defined on the "Risk Profile Field Definitions" tab of the Risk Profile Refresh Excel document provided. For the purpose of our review, we focused only on active risks that affect HUD at the entity level.

44 The program offices included, the Office of Lead Hazard Control and Healthy Homes, OCIO. the Office of Housing, the Office of Fair Housing and Equal Opportunity (FHEO), CPD, OCHCO, OCFO, the Office of Policy Development and Research, Ginnie Mae, and OGC.

45 Proposed risk response is defined as the proposed management process(es) and key controls that will be implemented to address the risk.

Management Reviews and Assessments Were Not Performed

We have reported since fiscal year 2015 on HUD's lack of conducting routine or timely management control reviews (MCR).[46] During fiscal year 2018, HUD did not conduct any routine or timely MCRs. Further, we noted that Front End Risk Assessment (FERA)[47] for its program areas were also not conducted.

The inconsistent performance of MCRs deprives management of an important monitoring tool that provides key feedback on the effectiveness and efficiency of departmental operations. The nonperformance of FERAs hinders management's ability to detect conditions that may adversely affect the achievement of program objectives and to provide reasonable assurance of financial reporting. Without the consistent performance of either of these evaluations, HUD may be unable to detect conditions that could adversely impact the achievement of program objectives, including effectiveness and efficiency of operations, in a timely manner. The lack of reviews impacts the reliability of HUD's financial reporting and its ability to comply with applicable laws and regulations, including OMB Circular A-123, Management's Responsibility for Enterprise Risk Management and Internal Control. For example, MCRs provide a basis for the HUD Secretary to report annually to the President and Congress, as required by the Federal Managers Financial Integrity Act (FMFIA), on the adequacy of management controls within HUD. Insufficient performance and monitoring of this process for all of HUD's program offices could prevent the Secretary from having an adequate basis when reporting on FMFIA.

In our fiscal year 2015 audit, we recommended that HUD revise its MCR policies and procedures to include clearer and more specific requirements, including accountability for nonperformance.[48] As of September 30, 2018, HUD had not completed the revision of policies for MCRs and FERAs, and as a result, the agency did have effective internal guidance for conducting the reviews. Management efforts to implement recommendations offered by OIG have been halted due to the transition of these functions from OCFO to Office of Strategic Planning and Management (OSPM) in fiscal year 2017. However, unclear delegation of roles and responsibilities continued to exist in fiscal year 2018. As late as September 2018, OSPM was unaware that the oversight and implementation of MCRs and FERA execution was its responsibility. Therefore, we have yet to note improved consistency or increased frequency of reviews, and prior-year OIG recommendations remained unresolved as of September 30, 2018.

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[46] An MCR is a detailed evaluation of the complete system of management controls in a functional area. Such a review will produce extensive documentation of controls and will include the testing of most if not all controls.

[47] A Front End Risk Assessment is a formal, documented review by management to determine the susceptibility of a new or substantially revised program or administrative function to waste, fraud, abuse, and mismanagement. Its purpose is to detect conditions that may adversely affect the achievement of program objectives and to provide reasonable assurance that the following goals will be met: (1) safeguarding of assets, (2) effectiveness and efficiency of operations, (3) reliability of financial reporting, and (4) compliance with applicable laws and regulations.

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

HUD Continued To Not Implement and Maintain Adequate Accounting and Financial Systems

The Chief Financial Officers Act of 1990 (CFO Act) states that the responsibilities of an agency CFO include developing and maintaining adequate accounting and financial systems and implementing agency asset management systems, including systems for cash management, debt collection, and property and inventory management and control. We continue to report a material weakness related to HUD's financial management system and noncompliance with FFMIA, as discussed in findings 3 and 7. While OCFO has made progress with the implementation of a new financial reporting system provided by its FSSP, OneStream, many manual processes continue to exist because HUD has been unable to retire legacy accounting systems as the program offices are dependent on them. Additionally, HUD's lack of system implementation impacts its compliance with OMB Circular A-123, Enterprise Risk Management, requirements. The Risk Management Model Maturity Assessment performed in 2018 found that in the category of data and technology,[49] HUD received a score of 20 of 100 percent, which was a "weak" classification. The assessment results indicated that HUD needs to define risk data governance, establish standards for risk data, and implement automated controls and compliance technology to store HUD data. In 2016, GAO's audit reported that HUD's management and governance weaknesses must be addressed to enable HUD to effectively modernize its financial systems.[50]

Although HUD's governance culture is now supported by current initiatives to improve its financial management, there continue to be weaknesses in data technology governance. HUD must implement and maintain financial systems in accordance with CFO Act requirements by collaborating effectively, addressing governance weaknesses, and remediating financial system issues.

HUD's Financial Management Maturity Weaknesses Continued

As reported in the prior year and based on the remaining financial management challenges facing HUD described in this finding and report, HUD's financial management maturity continued to be at "inadequate" or "basic" levels in the areas of (1) financial integrity and financial systems and (2) reporting, based on the Federal Financial Management Maturity Model.[51] HUD continued to reflect the examples outlined under the inadequate and basic levels, such as and most importantly (1) receives a modified opinion or disclaimer, (2) does not meet reporting deadlines and is unable to produce the cost of agency programs, and (3) uses legacy financial management systems.

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[49] Management of risk data that can be translated into meaningful risk information for stakeholders. It includes the development and deployment of risk management tools, software, databases, technology architecture, and systems that support risk management activities.

[50] GAO-16-656, HUD Needs to Address Management and Governance Weaknesses That Jeopardize Its Modernization Efforts, http://www.gao.gov/assets/680/678727.pdf

[51] Bureau of the Fiscal Service, U.S. Department of the Treasury, Federal Financial Management Maturity Model, https://www.fiscal.treasury.gov/fsservices/gov/fit/MaturityModelHandout.pdf. The model is a business tool developed to help a CFO self-assess the organization's level of financial management discipline, effectiveness, and efficiency. It centers on the "fitness" of an agency's financial management and can validate an agency's maturity against a standard framework and areas in which there is opportunity to improve.

HUD's continued financial management maturity weaknesses have not only contributed to the material weaknesses and significant deficiencies noted in our independent auditor's report, they have also impacted the integrity of HUD's financial reporting processes and contributed to HUD's disclaimer of opinion. HUD's financial management maturity weaknesses have resulted in many financial statement and note disclosure errors that have required frequent restatements, which continued in fiscal year 2018. For the fifth consecutive year, HUD will need to restate prior-year financial statements and note disclosures to correct errors that were not detected or prevented by HUD's internal controls. Frequent restatements to correct errors and disclaimers can undermine stakeholder trust and confidence.

Further, we have attributed the root cause of finding 2 to inadequate consideration of key accounting and financial rules and regulations. For example, the findings related to (1) non-GAAP budgetary accounting for CPD formula and disaster grants and (2) non-GAAP accounting for investments held by IHBG recipients are examples of how weak financial management maturity allowed noncompliant GAAP accounting to occur and continue in fiscal year 2018.

- *CPD's budgetary accounting for grants.* OCFO was not involved in the development of the mixed financial system (IDIS Online) to ensure that it complied with FFMIA and GAAP. This deficiency caused HUD to receive a qualified opinion in fiscal year 2013 and will contribute to HUD's disclaimer of opinion until the funds impacted are assessed to be immaterial. In an attempt to address the deficiency, programing changes were made to IDIS Online on a prospective basis for fiscal years 2015 forward but they were not applied to fiscal year 2014 and prior-year grant funds. As of September 30, 2018, and September 30, 2017, approximately $1.1 billion and $1.5 billion, respectively, in undisbursed obligations were impacted.[52]

- *Grant accounting for CPD disaster recovery.* An OIG field audit[53] performed to determine whether HUD CPD monitored and ensured that grantees complied with the 24-month statutory expenditure requirement contained in the Disaster Relief Appropriations Act, 2013, identified issues with (1) the recording of grants in LOCCS and (2) the grantees' recording of expenditures in the DRGR system. Specifically, two grantees had recorded total expenses in the DRGR system that exceeded what CPD had obligated for a grant round by $160 million. Five grantees recorded expenses totaling $435 million in DRGR before CPD executed a grant round amendment and after a grant round had expired. Finally, four grantees made more than $496 million in revisions to completed and revised vouchers in DRGR a year or more after they entered the initial voucher.

- *IHBG investments.* OCFO did not properly account for approximately $128.5 million in advanced payments to its IHBG grantees for investment because OCFO believes that these investments did not meet the criteria of an asset. In our analysis, we determined that (1) the investments do embody economic benefit or service because HUD receives its economic benefit or service when the investments are spent on an activity that fulfills

[52] Refer to finding 2 of this report for additional details.
[53] Full details on these findings can be found in audit memorandum 2018-FW-0802.

HUD’s mission, whereas money sitting in an investment account does not fulfill HUD’s mission, and (2) HUD controls access to the economic benefits through regulations over the investments, a depository agreement, and regulations on how the funds are spent once the investment period is over. OCFO provided a flawed accounting analysis that centered on NAHASDA regulations and did not adequately assess all aspects of the investments against GAAP.

In fiscal year 2018, HUD has begun the preliminary steps of implementing practices that are robust and supported by continuous process improvements with the execution of the CFO’s finance transformation plan and the Risk Management Model Maturity Assessment. As stated earlier, the assessment results identified weaknesses in several areas, including governance, reporting, monitoring, culture, and technology. Despite identifying the potential challenges and changing circumstances within the organization, it is crucial for management to implement corrective actions in response to identified financial reporting risks.

Conclusion

HUD’s financial management governance progressed during fiscal year 2018; however, more work is needed to substantially address all of the financial management weaknesses currently challenging HUD. HUD’s financial management structure was strengthened by filling leadership positions; however, some key personnel roles remained vacant within OCFO. Despite HUD’s making progress by approving a policy and procedure framework and developing other key policies and procedures, HUD continued to lack mature financial management governance practices and sufficient policies and procedures to fully update significant business process changes. Further, HUD management continued to not perform critical management reviews and assessments, including MCRs and FERAs, which impacts the assurance of program efficiency and operational effectiveness. HUD leadership has implemented an OMB A-123 ERM risk appetite into its annual risk assessment; however, management has not completed the appropriate actions to address identified weakness by assigning risk mitigation owners. Without delegation of risk response and implementation of additional internal controls, the identified risks will continue to impact reliable financial reporting. Further, the limited response to risks identified through the agencywide risk profile could put the agency at risk of noncompliance with laws and regulations, such as OMB Circular No. A-123, Management's Responsibility for Enterprise Risk Management and Internal Control.

As we have reported in prior-year audits, HUD continued the use of its outdated legacy financial systems, resulting in systematic errors and manual reporting processes that adversely impacted the reliability of financial data. OCFO had progressed with implementing a new financial reporting system, OneStream, which has helped with automating a substantial part of the financial statement preparation process. Conversely, HUD’s third quarter fiscal year 2018 financial statements and notes were misstated and missing required information.

Until the remaining weaknesses in HUD’s governance structure are remediated and HUD’s financial management processes have matured, OCFO’s unaddressed financial governance weaknesses will continue to hinder effective remediation of the material weaknesses, significant deficiencies, and instances of noncompliance with laws and regulations we have reported as of September 30, 2018.

Recommendations

Prior-year recommendations remained unimplemented and can be found in the Followup on Prior Audits section of this report. We offer the following new recommendations.

We recommend that the Chief Financial Officer

4A. Delegate responsibilities to the appropriate program office and assign risk owners to provide responses for the acceptance, mitigation, and elimination of risks identified in HUD's ERM risk profile.

4B. Develop, implement, and document internal controls in response to identified risks from HUD's ERM risk profile in compliance with OMB Circular No. A-123, Management's Responsibility for Enterprise Risk Management and Internal Control.

4C. Complete and issue final FERA policy to the Department and communicate the requirements within the policy to program offices in a timely manner.

We recommend that the Deputy Secretary

4D. Assign and communicate the responsibility of FERA policy implementation and oversight to ensure that program offices are performing FERAs on a routine and timely basis to ensure effectiveness and efficiency of operations at the HUD program level and compliance with HUD internal policy and procedure.

4E. Assign and communicate the responsibility of the MCR program policy, implementation, and oversight to ensure that program offices routinely conduct reviews to support a compliant internal control framework.

Finding 5: HUD Continued To Report Significant Amounts of Invalid Obligations

Deficiencies in HUD's process for monitoring its unliquidated obligations and deobligating balances tied to invalid obligations continued to exist. We identified $65.8 million in obligations that HUD determined needed to be closed out and deobligated during the fiscal year that remained unprocessed as of September 30, 2018. We also identified $47.6 million in obligations that were inactive,[54] potentially indicating additional invalid obligations. We attributed these deficiencies to ineffective monitoring efforts and the inability to promptly process contract closeouts. Lastly, we noted that as of September 30, 2018, HUD had not implemented prior-year recommendations to deobligate $576.4 million in funds. We attributed the root cause of these conditions to weaknesses with HUD's open obligation review (OOR) and with program office monitoring of obligations. As a result, HUD's unobligated balance from prior-year budget authority and related line items on the statement of budgetary resources were understated by at least $65.8 million and potentially understated by up to $689.8 million.

HUD's Annual Departmentwide Obligation Review and Certification Process Had Weaknesses

The annual departmentwide OOR and certification process is an essential part of HUD's internal controls over its funding and accurate financial reporting. This review gives OCFO assurance that its end of the fiscal year obligation balance is valid and accurately valued. It is critically important that the program offices thoroughly review all open obligations to ensure that remaining unliquidated obligations are still valid and needed. Our review identified weaknesses with the OOR; specifically, a failure to complete OOR certifications in a timely manner, deobligating obligations marked for deobligation as of September 30, 2018, and retaining obligations that are inactive and possibly invalid.

- *Failure to complete the OOR markup phase in a timely manner*. Four offices struggled to complete their review portion of the OCFO coordinated review by the annual deadline that OCFO required. The OOR web-based application was available for all users to review and mark obligations as "retain" or "deobligate" beginning March 31, 2018, until July 13,[55] 2018; however, PIH, CPD, the Office of Housing, and the Office of Fair Housing and Equal Opportunity (FHEO) missed the July 13, 2018, deadline. These four offices accounted for 65,732, or 95 percent, of the 69,257 OOR obligations required to be reviewed (that is, obligations over the review threshold[56]).

[54] We define an obligation as inactive if a disbursement has not been made within a reasonable amount of time. This time varies based on program area and applicable criteria.

[55] We noted inconsistencies with the deadlines included in the fiscal year 2018 OOR memorandum; therefore, to be conservative in our approach, we used the latest submission deadline available, July 13, 2018, as the required final deadline.

[56] The threshold to be included in the OOR for administrative and program obligations is $24,491 and $101,214, respectively.

- *Obligations marked for deobligation but not beobligated as of September 30*. During the fiscal year 2018 audit, we reviewed 3,528 HUD-identified obligations totaling $115 million marked for deobligation by the program offices. Of these, 1,162 obligations with remaining balances of $65.8 million, or 57 percent of the total value, were not closed out and deobligated by the end of the fiscal year.[57]

- *Retained obligations that are inactive and possibly invalid*. Our review of retained obligations with no disbursement activity since March 31, 2016, identified 547 obligations with remaining balances totaling $47.6 million that have had no activity (disbursements) since at least fiscal year 2016. The program offices marked these obligations as "retain" during the markup phase. However, a lack of recent disbursement activity indicates that the obligations are inactive, are potentially invalid, and require further review. In reviewing the justifications entered into the OOR for the identified inactive obligations, we found 124 records totaling $10.9 million, or 23 percent of all obligations in question, using some form of the justification, "this is an active contract." However, because these obligations have not had disbursements in 2 or more years, these justifications appear contradictory and raise the question as to whether these obligations were adequately reviewed before being marked as "retain."

We attributed the conditions identified to weaknesses with the OOR process and overall weaknesses with the monitoring of obligations within the program offices. Specifically, we noted the following two causes: (1) OOR review assignments are too voluminous to be completed only annually and (2) the OOR lacks adequate policies and procedures.

- *OOR review assignments are too voluminous to be completed only annually.* In its current design, the OOR required program offices to review 69,257 obligations totaling $33.6 billion in a 3-month period (quarter three of the fiscal year) and have all marked deobligations processed by September 30, 2018. As previously noted, program offices struggled to process all marked deobligations as required, which has been a consistent problem for the past 5 consecutive years.[58] We attributed this issue to the frequency in which the OOR is conducted. The continued struggles with an annual review process indicate that the process could be improved by shifting to a review that occurs more frequently than annually. A review process that occurs more frequently with smaller, more manageable review assignments could ease the yearend burden on program areas and improve the OOR as a control over obligation balances that occurs throughout the year instead of only once a year.

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[57] Refer to Appendix B – Departmentwide Obligation Review – Schedule of Recommended Deobligations.

[58] HUD OIG audit reports 2018-FO-0004, 2017-FO-0003, 2016-FO-0003, 2015-FO-0002, and 2014-FO-0003 identified $61.8 million, $34.6 million, $30.7 million, $27.3 million, and $43 million in unprocessed deobligations, respectively.

- *HUD's OOR lacks adequate policies and procedures.* HUD's departmentwide policy regarding the OOR is limited to one section in HUD Handbook 1830.2, REV-6, technical guides to the web-based application and the annual memorandum announcing the review to the Department.[59] OCFO lacked comprehensive, detailed procedures that applied to the entire Department, including (1) established roles and responsibilities of OCFO, OCPO, and program offices; (2) standard timeframes to conduct the review; and (3) internal controls to ensure reliability of the review. OCFO developed standard operating procedures during fiscal year 2018; however, they applied only to the roles and responsibilities specific to OCFO accounting.

  In response to our findings, multiple programs stated that obligations marked for deobligation that had not been deobligated by the end of the fiscal year had been submitted to the Office of the Chief Procurement Officer (OCPO) for deobligation. Delays within OCPO in the processing of deobligations were causing the obligations to remain recorded. Due to insufficient timing of the information received, we were unable to verify this information. However, we noted that OCFO's standard operating procedures did not include performing followup on the obligations sent to OCPO, as part of the OOR process, to determine the status or whether sufficient information was forwarded to ensure timely deobligation.

As a result of these weaknesses, HUD's unobligated balance from prior-year budget authority and related line items on the statement of budgetary resources were understated by at least $65.8 million due to unprocessed deobligations and potentially understated by an additional $47.6 million due to inactive invalid obligations as of September 30, 2018. Further, weaknesses in internal controls and monitoring of HUD's unpaid obligation balances prevent HUD from maximizing the use of its budgetary resources that directly benefit the taxpayers and those in need. See appendix B.

Prior-Year Recommendations Had Not Been Implemented

We noted that as of September 30, 2018, prior-year recommendations regarding deobligation amounts of $576.4 million were outstanding. Therefore, HUD's unobligated balance from prior-year budget authority on the statement of budgetary resources related to prior-year unimplemented recommendations was potentially understated by $576.4 million. Refer to table 1 below.

[59] As a result of prior-year recommendation 2018-FO-0004-008-A, HUD's Accounting, Monitoring, and Analysis Division developed a standard operating procedure for the OOR, dated May 2018. Our review did not find this document to be comprehensive enough to remediate the identified OOR weaknesses.

Table 1		
Prior-year recommended deobligations not implemented as of September 30, 2018		
Office	**Program**	**Amount**
CPD, Housing, FHEO	OOR – retained inactive obligations	$285.9 million
CPD	Homeless assistance	109.4 million
Ginnie Mae	Program contracts	104.1 million
Housing	Section 202-811	67.8 million
CPD	Emergency Solutions Grant	4.9 million
CPD	Neighborhood Stabilization Program	3.7 million
Housing	Section 236	.6 million
Total:		**576.4 million**

Conclusion

HUD's processes for (1) monitoring the validity and need for its unliquidated obligations and (2) processing of deobligations continued to not be fully effective during fiscal year 2018. HUD did not close out all of the obligations identified as invalid by the end of the fiscal year, resulting in HUD's unobligated balance from prior-year budget authority and related line items on its consolidated statement of budgetary resources to be understated by $65.8 million and potentially understated by an additional $47.6 million in obligations that have had no disbursement activity since at least fiscal year 2016. We also noted that as of September 30, 2018, HUD had not implemented prior-year recommendations for $576.4 million, which further contributed to a potential understatement. In total, HUD's consolidated statement of budgetary resources was understated by at least $65.8 million and potentially understated by up to $689.8 million due to invalid obligations. Refer to table 2 below.

Table 2	
Program	**Amount**
Annual departmentwide obligations review – obligations with no disbursements since 2016	$47.6 million
Annual departmentwide obligations review – marked for deobligation but not deobligated as of 9/30/18	65.8 million
Prior-year unimplemented recommendations	576.4 million
Total	**689.8 million**

Recommendations

We recommend that the Chief Financial Officer

5A. Conduct the OOR more frequently than annually to ensure that all obligations are adequately reviewed and deobligations are processed by the end of the fiscal year.

5B. Develop departmental policy that outlines the open obligation review process, to include (1) internal controls, (2) timeframes, and (3) roles and responsibilities of OCFO, OCPO, and program offices. These policies must outline sufficient internal controls in place to ensure that the Secretary can certify that all of HUD's obligations are valid as of the end of the fiscal year.

5C. Update standard operating procedures on the departmentwide unliquidated obligations review to conduct a routine review of justifications provided by the program offices for retained obligations, while ensuring that they are for a bonafide need and to support the annual certification made by the Secretary on open obligations.

5D. As part of the OOR process, conduct monitoring activities of obligations sent to OCPO for deobligation by developing a mechanism to routinely track the status, to include key information, such as but not limited to the owner (program), date transmitted to OCPO, point of contact, last contact date, and current status. OCFO should use this information to ensure that all information has been communicated among all parties involved to enable timely deobligation.

We recommend that the Assistant Secretary for Community Planning Development

5E. Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $7,517,486 in 187 program obligations and $62,183 in 9 administrative obligations marked for deobligation as of September 30, 2018.

5F. Review the 473 identified inactive retained obligations with remaining balances totaling $43,005,703 and close out and deobligate amounts tied to obligations that are no longer needed.

We recommend that the Assistant Secretary for Housing-Federal Housing Commissioner

5G. Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $51,396,319 in 735 administrative obligations and $5,350,112 in 68 program obligations marked for deobligation as of September 30, 2018.

5H. Review the 65 identified inactive retained obligations with remaining balances totaling $4,310,534 and close out and deobligate amounts tied to obligations that are no longer valid or needed

We recommend that the General Deputy Assistant Secretary for Public and Indian Housing

5I. Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $588,694 in 12 administrative obligations marked for deobligation as of September 30, 2018.

5J. Review the three identified retained inactive obligations with remaining balances totaling $78,069 and close out and deobligate amounts tied to obligations that are no longer valid or needed.

We recommend that the Assistant Secretary for Fair Housing and Equal Opportunity

5K. Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $168,198 in 29 obligations marked for deobligation as of September 30, 2018.

5L. Review the five identified retained inactive obligations with remaining balances totaling $110,224 and close out and deobligate amounts tied to obligations that are no longer valid or needed.

We recommend the Chief Human Capital Officer

5M. Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $574,511 in 79 administrative obligations marked for deobligation as of September 30, 2018.

We recommend that the Director of the Office of Equal Employment Opportunity

5N. Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $106,962 in 30 administrative obligations marked for deobligation as of September 30, 2018.

We recommend that the Director of the Office of Lead Hazard Control and Healthy Homes

5O. Review the one identified retained inactive obligation with a remaining balance totaling $60,395 and deobligate amounts that are no longer valid or needed.

We recommend that the Acting General Deputy Assistant Secretary for Policy Development and Research

5P. Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $54,909 in 13 administrative obligations marked for deobligation as of September 30, 2018.

Finding 6: HUD's Computing Environment Controls Had Weaknesses

HUD's computing environment, data centers, networks, and servers provide critical support to all facets of its program, mortgage insurance, financial management, and administrative operations. We audited the general and application controls over the internet server general support system (GSS) and selected information systems that support the preparation of HUD's financial statements. HUD did not ensure that controls over its computing environment fully complied with Federal requirements. Specifically, we identified weaknesses related to HUD's internet server GSS and the OneStream and GrantSolutions applications maintained by shared service providers. The weaknesses identified with the internet server GSS occurred because HUD did not initiate actions in a timely manner to address known vulnerabilities and did not provide sufficient oversight and guidance to its IT support contractors. For OneStream and GrantSolutions, the weaknesses occurred because the shared service provider believed that it had an alternative security measure in place and HUD believed that its current processes were adequate. Without adequate controls, there is no assurance that HUD's financial management applications and the data within them were adequately protected.

Information System Control Weaknesses Were Identified With the Internet GSS

The internet GSS allows HUD to logically connect to the public internet or other external connections, provides remote connectivity to HUD IT systems for authorized users (including approved business partners) and the public (that is, to public-facing HUD web servers) through controlled and monitored access points, and provides protection against unauthorized access to HUD facilities through the internet. Our review identified weaknesses related to (1) the lack of full, functional testing of disaster recovery capabilities, (2) the use of outdated security protocols within HUD's computing environment, (3) cryptographic settings that were disabled without proper approvals, (4) inadequately segregated duties for privileged users with access to servers hosting two of HUD's major financial applications, and (5) inadequate access controls over privileged users.[60]

Disaster Recovery Exercises Did Not Fully Test Critical Applications and System Performance

We evaluated the results of HUD's disaster recovery exercise conducted in May 2018 and determined that the functionality of critical applications was not fully tested and verified and system performance was not measured using equipment located at the disaster recovery facility. Operating systems and application data were restored from alternate media and validated, but the critical applications were not verified through transaction and batch processing. This condition occurred because HUD believed that it could not include full functional testing in the disaster recovery contract because the previous disaster recovery facility had limited capabilities to handle full, functional testing of the critical applications and measurement of systems performance. Without full disaster recovery fail-over testing, HUD has limited assurance that

[60] Privileged users are users whose authorized access provides a capability to alter the properties, behavior, or control of the information system or network. This access allows more rights and permissions than those given to standard business users.

HUD systems and critical applications will function as intended when activated at an alternate facility during an actual emergency situation.

HUD Uses Outdated Security Protocols

HUD allows the use of outdated security protocols in its computing environment. This condition occurred because OCIO had not completed its efforts to work with the owners of those applications still using the outdated protocols to upgrade to current requirements. By not upgrading to current cryptographic protocol standards, HUD increased the risk that its data could be intercepted and accessed by unauthorized individuals.

HUD Disabled a Cryptographic Setting for HUD Workstation Client

HUD disabled a cryptographic module setting for HUD workstation[61] client to client-server[62] communications within the local area network[63] and did not obtain a waiver before disabling the setting. Protection of a cryptographic module within a security system is necessary to maintain the confidentiality and integrity of the information protected by the module. HUD disabled the setting because (1) OCIO still has users that connect to HUD systems using outdated security protocols that do not support the algorithms and (2) HUD believes that enabling the setting would negatively impact system performance. However, the operational impact of implementing Federal Information Processing Standard compliant encryption for hashing[64] and signing had not been tested for compatibility with legacy applications that are critical to HUD operations. HUD did not follow the procedures necessary to obtain a waiver because it felt that the waiver it processed internally in 2010 was sufficient. HUD's workstations are used to access internal and external applications by HUD users to conduct HUD business that involves the processing of sensitive and financial information. By not enabling the cryptographic configuration setting, HUD cannot ensure that its computer and telecommunication systems that use cryptographic modules provide an acceptable level of security for the given application and environment.

Segregation of Duties for Privileged Users on Servers Hosting IDIS and DRGR Was Not Adequate

Segregation of duties was not adequately enforced for privileged users with access to the servers that host IDIS and DRGR. Separation of duties is a classic security method to manage conflict of interest, the appearance of conflict of interest, and fraud. It restricts the amount of power held by any one individual. It puts a barrier in place to prevent fraud that may be perpetrated by one individual. This condition occurred because the job categories used by HUD's IT support contractor were broad and HUD did not ensure that the contractor's implementation complied with HUD policies and industry best practices. Inadequately segregated duties increase the risk

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61 Workstations are intended primarily to be used by one person at a time. They are commonly connected to a local area network and run multiuser operating systems.

62 A client is a piece of computer hardware or software that accesses a service made available by a server. The server is often (but not always) on another computer system, in which case the client accesses the service by way of a network.

63 A local area network is a computer network that interconnects computers within a limited area, such as a residence, school, laboratory, university campus, or office building.

64 Hash - A hash is a function that converts an input of letters and numbers into an encrypted output of a fixed length.

that erroneous or fraudulent transactions could be processed, which could lead to inaccurate information flowing into HUD's financial statements. Inadequately segregated duties also increase the risk that improper program changes could be implemented, computer resources could be damaged or destroyed, and errors and wrongful acts may go undetected because the activities of one individual would not serve as a check on the activities of another.

Access Controls of Servers Hosting IDIS and DRGR Were Not Properly Authorized in Accordance With HUD Policies

We reviewed access controls for the servers that host IDIS and DRGR and found that access controls for privileged users were not always properly authorized in accordance with HUD policies. This condition occurred because some of the accounts were established before current requirements and HUD did not provide clear guidance to its IT support contractors regarding account-naming conventions. Inadequate access controls reduce the reliability of computerized data and increase the risk of destruction or inappropriate disclosure of data. By obtaining access to system-level resources, an individual could circumvent security controls to read, add, delete, modify, or exfiltrate critical or sensitive business information or programs. Further, authorized users could gain unauthorized privileges to conduct unauthorized actions or to circumvent edits and other controls built into the application programs.

Information Security Risks Were Identified in OneStream

We also found that the interconnection security agreement (ISA) and memorandum of agreement (MOA) between HUD and Treasury was out of date. The ISA specifies the technical and security requirements of an interconnection, and the MOA defines the responsibilities of the participating organizations. According to the National Institute of Standards and Technology Special Publication 800-47, a system interconnection is defined as the direct connection of two or more IT systems for the purpose of sharing data and other information resources. Organizations can connect their IT systems using a dedicated line or over a public network (e.g., the Internet). Data transmitted over a public network can be intercepted by unauthorized parties, however, necessitating the use of authentication and encryption to ensure data confidentiality and integrity. HUD users access OneStream via the Internet with their userIDs and passwords. Therefore, there exists an interconnection between HUD and OneStream. Our review also found that the most recent version of the document was not signed in a timely manner, the document was missing required information and requirements, and the document contained inaccurate references to HUD policies and requirements. These conditions occurred because OCIO deferred responsibility for updating the information in the ISA and MOA to the program offices and system owners and errors were made in the document.

The intent of the MOA and ISA is to provide the appropriate authorizing officials a detailed account of the security controls, such that an educated risk-based decision can be made as to whether to permit the described connections. Interconnecting IT systems can expose the participating organizations to risk. If the interconnection is not properly designed, security failures could compromise the connected systems of HUD and Treasury and the data that they store, process, or transmit. Similarly, if one of the connected systems is compromised, the interconnection could be used as a conduit to compromise the other system and its data. The potential for compromise is underscored by the fact that, in most cases, the participating organizations have little or no control over the operation and management of the other party's system. Therefore, financial data residing on the IT systems could be at risk of compromise, resulting in inaccurate financial statements and note disclosures.

Information System Security Risks Were Identified in GrantSolutions

The President's fiscal year 2007 budget established the Grants Management Line of Business (GMLoB), a Presidential E-Government Initiative, to create a common solution for grants management. OMB selected GrantSolutions, a grants center of excellence within the United States Department of Health and Human Services, as one of the consortia leads of the GMLoB initiative to provide grants management services to Federal departments and agencies, one of which is HUD. The Grants Management and Oversight Division within HUD OSPM provides oversight and policy responsibility for HUD's grant programs. In fiscal year 2017, approximately $303 million was processed through GrantSolutions.

Controls within GrantSolutions to ensure least privilege[65] were not enforced. HUD has 220 users of the GrantSolutions application, and 3 users were assigned roles, which they did not need to perform their duties. We also found that the GrantSolutions policies regarding the assignment of critical roles were not consistent. This condition occurred because the monitoring process of role and account assignment was not sufficient. Dividing duties diminishes the likelihood that errors and wrongful acts will go undetected because the activities of one group or individual will serve as a check on the activities of the other. Inadequately segregated duties, conversely, increase the risk that erroneous or fraudulent transactions could be processed, improper program changes could be implemented, and computer resources could be damaged or destroyed. Misuse of privileged functions, either intentionally or unintentionally, by authorized users or by unauthorized external entities that have compromised information system accounts is a serious and ongoing concern and can have significant adverse impacts on organizations and their financial statements. When we brought this matter to the attention of OSPM, it reevaluated the users' roles and job responsibilities and agreed to remove the extraneous roles from the users' profile. In addition, OSPM agreed to increase the regular monitoring of user role and account assignments and update the GrantSolutions policies regarding the assignment of critical roles.

OSPM has not conducted a recertification of users accessing the GrantSolutions system since its launch during September 2016. Recertification of users accessing the GrantSolutions systems had not been conducted within the past 2 years because OSPM and its Grants Management and Oversight (GMO) Division believed that it had alternative practices in place that served as a sufficient substitute for the recertification process. When annual recertifications are not conducted as part of the continuous monitoring process, GMO cannot be sure that those with user accounts and access to the GrantSolutions system have a continued, valid need for access and that their level of access is appropriate for their job function. While GrantSolutions' role-based privileges limit the actions of a user to those appropriate for the role assigned, if that role assignment is no longer appropriate, the user can intentionally or unintentionally read, add, delete, modify, or exfiltrate data or execute changes that are outside his or her current span of authority until his or her role in GrantSolutions is changed to reflect his or her new authority.

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65 Least privilege is the principle requiring that each subject be granted the most restrictive set of privileges needed for the performance of authorized tasks.

Information Security Control Weaknesses Were Previously Identified Related to the Implementation of the New Core Project

In September 2017, we reported that although transaction processing using the New Core Financial Management Solution had improved, challenges and weaknesses remained.[66] Although HUD had improved from what we found during our fiscal year 2016 audit work, HUD (1) continued to experience some weaknesses in transaction processing, (2) could not fully support the balances recorded in its general ledger, and (3) did not fully reconcile data between the HUD Central Accounting Program System (HUDCAPS) and its general ledger.

We issued six recommendations, and HUD completed actions to address four of the recommendations. The two remaining recommendations to update yearend closing procedures and resolve the unreconciled subledger differences identified after October 1, 2016, are scheduled to be completed during January 2019.

In February 2017, we reported that HUD's transition to an FSSP failed to meet expectations.[67] A year after the transition, HUD had inaccurate data resulting from the conversions and continued to execute programmatic transactions using its legacy applications. We issued 13 recommendations to address the identified issues. HUD has completed actions to address 10 of the recommendations. No management decisions were reached for two of the recommendations in regard to reevaluating the functionality initially planned for budget formulation, cost accounting, property management, and the consolidation of HUD's financial statements and senior management's role in implementing financial management improvement initiatives-projects moving forward. The one remaining recommendation regarding the project plans for the decommissioning of HUDCAPS and the Enterprise Data Warehouse is overdue as it was scheduled to be completed in April 2018.

During fiscal year 2016, we audited the implementation of phase 1, release 3,[68] of the New Core Project and determined that HUD had rushed the implementation. HUD had unresolved data conversion errors and inaccurate funds management reports and lacked a fully functional data reconciliation process. In addition, the performance of the New Core Interface Solution (NCIS) was not monitored, tracked, or measured, and controls over processing errors within Oracle Federal Financials were routinely bypassed. These conditions occurred because HUD did not move the implementation date when issues were identified during system testing to allow time to resolve the issues, development of the custom reports was not far enough along to allow full system testing, development of the reconciliation tool could not be completed before the

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[66] Audit Report 2017-DP-0003, New Core Project: Although Transaction Processing Had Improved Weaknesses Remained, issued September 28, 2017

[67] Audit Report 2017-DP-0001, HUD's Transition to a Federal Shared Service Provider Failed To Meet Expectations, issued February 1, 2017, and the material weakness, "HUD's Financial Management System Weaknesses Continued," included in Audit Report 2018-FO-0004, Additional Details To Supplement Our Fiscal Years 2017 and 2016 (Restated) U.S. Department of Housing and Urban Development Financial Statement Audit, issued November 15, 2017

[68] Audit Report 2016-DP-0004, HUD Rushed Implementation of Phase 1, Release 3, of the New Core Project, issued September 20, 2016

scheduled implementation date, and time did not permit the establishment of performance metrics. As a result, in June 2016, unresolved data conversion errors were estimated at an absolute value of more than $9 billion, HUD's funds management reports contained inaccurate data, the newly completed status of funds reconciliation report indicated that there was an absolute value of $4.5 billion in differences between HUDCAPS and Oracle Federal Financials, and it was difficult to tell whether NCIS met user needs and business process requirements.

We issued six recommendations, and HUD has completed actions to address four of the recommendations. The two remaining recommendations, related to correction of the data conversion errors and reviewing custom reports for accuracy, are overdue as they were scheduled to be completed during December 2017.

Information System Control Weaknesses Previously Identified in the Fiscal Year 2017 Federal Information System Controls Audit Manual General Support System Review

During fiscal year 2017, we audited the general controls over HUD's computing environment for compliance with HUD IT policies and Federal information system security and financial management requirements. We focused our audit work on the effectiveness of general controls over HUD's intranet GSS. The intranet GSS consists of web, file transfer protocol, and networking devices that support HUD's ability to provide information and services to the public.

In March 2018, we reported that HUD did not ensure that controls over the intranet GSS fully complied with Federal requirements and HUD's own internal policies.[69] Specifically, weaknesses within the intranet GSS were not properly tracked or remediated in a timely manner, GSSs were not reauthorized to operate, offline backup storage for HUD's data centers did not exist, unauthorized changes in asset and device inventory could not be identified, an unsecured file transfer protocol was used, and access controls were inadequate. These conditions occurred because of OCIO's insufficient oversight, use of nonspecific IT security procedures, belief that existing backup procedures and measures were sufficient, lack of resources needed to enable detection of unauthorized devices on its network, belief that using an unsecure protocol was a low risk because it was used to transfer files internally within HUD's infrastructure and behind HUD's firewall, and failure to review user accounts for compliance with account management requirements. As a result, HUD had various weaknesses with system controls and security management and did not ensure that general controls over its financial systems and its computing environment fully complied with Federal requirements. Without effective controls in place, HUD could not ensure that the systems and network would perform as intended to support its mission and generate accurate financial statements.

We issued 18 recommendations to address the weaknesses identified. HUD has completed the actions needed to close nine of the recommendations. Corrective actions for the remaining nine recommendations are scheduled to be completed by December 31, 2018.

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[69] Audit Report 2018-DP-0003, Fiscal Year 2017 Review of Information Systems Controls in Support of the Financial Statements Audit, issued March 9, 2018

Conclusion

HUD's computing environment provides critical support to all facets of its program, mortgage insurance, financial management, and administrative operations. During fiscal year 2018, as in prior years, we continued to identify information systems control weaknesses that could negatively affect HUD's ability to accomplish its assigned mission, protect its data and IT assets, fulfill its legal responsibilities, maintain its day-to-day functions, and generate accurate financial statements. As a result, we continue to report HUD's computing environment as a significant deficiency.

Recommendations

Recommendations related to our fiscal year 2018 information systems audits will be included in separate OIG audit reports. Therefore, no recommendations are reported here.

Compliance With Laws, Regulations, Contracts, and Grant Agreements

The following section is our report on HUD's compliance with laws, regulations, contracts, and grant agreements. We tested HUD's compliance with laws, regulations, governmentwide policies, and provisions of contract and grant agreements that could have a direct and material effect on the financial statements. In fiscal year 2018, we found instances in which HUD did not comply with laws and regulations that could have a direct and material effect on the financial statements and any other laws, regulations, and governmentwide policies identified in OMB audit guidance.

Our consideration of HUD's internal controls and our testing of its compliance with laws, regulations, governmentwide policies, and provisions of contract and grant agreements were not designed to and did not provide sufficient evidence to allow us to express an opinion on such matters and would not necessarily disclose all matters that might be instances of noncompliance with laws, regulations, governmentwide policies, and provisions of contract and grant agreements. A description of the scope of our testing of compliance with provisions of laws, regulations, contracts, and grant agreements is included in the Scope and Methodology section of this report.

Finding 7: HUD's Financial Management System Did Not Comply With the Federal Financial Management Improvement Act

In fiscal year 2018, we noted a number of instances of FFMIA noncompliance within HUD's financial management system. HUD's continued noncompliance with FFMIA was due to a high volume of material weaknesses, ineffectively designed and operating key internal controls over financial reporting, and longstanding issues related to component and program offices' system weaknesses that remained unresolved.

HUD'S FFMIA Noncompliance Continued in Fiscal Year 2018

FFMIA, section 803(a), requires CFO agencies to establish and maintain financial management systems that substantially comply with (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) USSGL at the transaction level. FFMIA also requires agencies and their auditors to determine annually whether an agency's financial management system (including primary or general ledger accounting systems and subsidiary or "mixed" systems) complies with those requirements.

As of September 30, 2018, we noted instances in which HUD did not comply with the three section 803(a) elements of FFMIA. We tested compliance with FFMIA in accordance with OMB Circular A-123, Appendix D, Compliance with the Federal Financial Management Improvement Act of 1996.[70] HUD also concluded that the agency and its financial management system did not comply with each element of FFMIA as of September 30, 2018. Refer to table 3 below for details.

Table 3
Compliance with section 803(a) elements of FFMIA

	Agency	Auditor
1. System requirements	Lack of compliance noted	Lack of compliance noted
2. Accounting standards	Lack of compliance noted	Lack of compliance noted
3. USSGL at transaction level	Lack of compliance noted	Lack of compliance noted

For areas of FFMIA noncompliance, each agency must identify remediation activities that are planned and underway, describing target dates and offices responsible for bringing systems into compliance with FFMIA.[71] These details are included in HUD's 2018 agency financial report (AFR).

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70 OMB Memorandum M-13-23 (OMB Circular A-123, appendix D)
71 OMB Circular A-136, Revised

In addition, when auditors disclose a lack of compliance with one or more of the section 803(a) requirements, FFMIA requires that auditors provide additional details regarding the noncompliance.[72] The details about systems not in compliance with FFMIA, responsible parties, recommendations, primary causes, and HUD's intended remedial actions are included below by FFMIA section 803(a) element(s).

Systems That Do Not Comply With Federal Financial Systems Requirements

New Core Interface Solution
NCIS did not comply with Federal financial system requirements. Specifically, NCIS did not capture or record required general ledger account transaction information to enable traceability between program accounts and the general ledger. NCIS is a custom-developed system owned by HUD and hosted by Oracle Managed Cloud Services. NCIS performs the extract, transform, and load functions, as well as a variety of error-processing, reconciliation, and interface file management functions to support the interface of HUD systems with ARC systems. OCFO is responsible for NCIS, a key interface between HUD's legacy systems and the general ledger, ARC's Oracle Federal Financials. NCIS has an outsized role in many key processes and, therefore, is tied to many material weaknesses. NCIS will be unable to comply with FFMIA until the remediation of related material weaknesses.

Systems That Do Not Comply With Federal Financial Systems Requirements and Federal Accounting Standards

Single Family Mortgage Asset Recovery Technology
The Office of Housing is responsible for the Single Family Mortgage Asset Recovery Technology (SMART) application, a loan-servicing system that services several programs. SMART did not comply with Federal financial system requirements and Federal accounting standards due to a lack of third-party controls over the timely and accurate processing of promissory notes, mortgage instruments, and partial claims. The Office of Housing has taken steps to address FFMIA noncompliance. For example, the Office of Housing incorporated a performance requirement measuring partial claims collection into a subsequent performance work statement. Improving contract performance measures and additional remediation efforts were pending OIG verification as of August 2018.

Single Family Asset Management System
The Office of Housing is responsible for the Single Family Asset Management System (SAMS). SAMS is a financial management system that performs a full range of financial oversight activities in support of HUD's Single Family Property Disposition program (section 204(g)).

SAMS did not comply with Federal financial system requirements and Federal accounting standards due to issues related to monitoring unliquidated obligation balances and inaccurate undelivered order balances. The Office of Housing was continuing work to address these issues as of August 2018.

[72] OMB Bulletin 19-01, Audit Requirements for Federal Financial Statements

Systems That Do Not Comply With Federal Accounting Standards and the U.S. Standard General Ledger at the Transaction Level

Integrated Disbursement and Information System Online

IDIS Online does not comply with applicable Federal accounting standards and USSGL at the transaction level. CPD is responsible for IDIS. IDIS is noncompliant with FFMIA due to the use of the FIFO method to account for grant disbursements. We previously recommended that HUD modify IDIS to account for grant disbursements by the specific identification method and configure the system to record transactions in compliance with USSGL. While system updates to address FFMIA noncompliance going forward were completed in fiscal year 2018, CPD's decision to eliminate FIFO prospectively only for fiscal year 2015 and future grants will result in lingering noncompliance until the amounts subject to FIFO become immaterial.

Systems That Do Not Comply With Financial System Requirements, Federal Accounting Standards, and the U.S. Standard General Ledger at the Transaction Level

Disaster Recovery Grant Reporting System

CPD is responsible for the DRGR system, an internet-based system supporting the Community Development Block Grant Disaster Recovery program and other special appropriations, which does not comply with Federal financial system requirements, Federal accounting standards, and USSGL at the transaction level due to system weaknesses and insufficient monitoring of invalid or expired obligations and issues with grantees' recording of Disaster Recovery program expenditures. We have recommended that CPD make changes to the DRGR application and make additional process improvements to address issues related to disaster grant activity.[73] CPD plans to address DRGR FFMIA noncompliance with policies and procedures to monitor inactive or expired obligations and is working with OIG to develop actions responsive to OIG audit memorandum 2018-FW-0802, and CPD estimates that remediation will be complete by December 31, 2020.

Tenant Rental Assistance Certification System

A 2017 FFMIA compliance review noted that the Tenant Rental Assistance Certification System (TRACS) is not compliant with (1) Federal financial management system requirements, (2) applicable Federal accounting standards, and (3) USSGL at the transaction level. The Office of Housing is responsible for the TRACS application. Implemented in 1993, TRACS is the official contract management repository for the Office of Multifamily Housing Programs' rental assistance project-based contracts, including budget projections and funding for contracts. TRACS is designed to process subsidy contracts, tenant rental assistance information, and owner requests for payment (vouchers) for project-based programs. TRACS does not comply with Federal financial system requirements, Federal accounting standards, or USSGL at the transaction level. TRACS issues include noncompliance with funds control policies and procedures, weaknesses in monitoring unliquidated obligations, and a failure to comply with improper payment requirements related to HUD's Rental Housing Assistance Programs (RHAP).

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[73] See finding 2 in this report.

The Office of Multifamily Housing Programs plans to address TRACS noncompliance through system enhancements it expects to implement by November 2018.

Ginnie Mae Financial and Accounting System

We noted that the Ginnie Mae Financial and Accounting System was noncompliant with the three section 803(a) elements of FFMIA as of September 30, 2018. Ginnie Mae's noncompliance stems from material weaknesses that include an inability to properly account for nonpooled loan assets from Ginnie Mae's defaulted issuers' portfolio. While progress was made during fiscal year 2018, Ginnie Mae will need to remediate unresolved material weaknesses to address FFMIA noncompliance. Ginnie Mae plans to resolve noncompliance with the implementation of a subledger database "loan-level accounting" system in Ginnie Mae's production environment in 2019.

Federal Asset Management Enterprise System

FAMES is noncompliant with the three section 803(a) elements of FFMIA (including internal use software) that were not auditable as of September 30, 2018. While OA is responsible for FAMES, poor coordination between HUD program offices and competing priorities have left the Department without a working property management system since 2012. We have previously recommended that HUD address property system and process weaknesses that rendered the former system Facilities Integrated Resource Management System (FIRMS) inoperable in 2012 and establish and maintain a complete and accurate property inventory. During fiscal year 2019, OA plans to establish and maintain a property inventory in FAMES and implement an Oracle fixed-asset module through its shared service provider to accurately account for internal use software.

Conclusion

HUD's financial management system did not comply with FFMIA as of September 30, 2018. Specifically, we noted instances in which HUD did not comply with the three section 803(a) elements of FFMIA.

The impact of HUD's system limitations is greater than noncompliance with the FFMIA framework. The identified system deficiencies identified as instances of FFMIA noncompliance and their impacts are further described throughout this report as contributing to a number of material weaknesses.

Recommendations

Prior-year recommendations regarding this finding remained open and can be referred to in the Followup on Prior Audits section of this report. We have no new recommendations in this report.

Finding 8: HUD Did Not Comply With the Debt Collection Improvement Act

HUD did not comply with DCIA as amended. The Act required that HUD refer delinquent debts to the Treasury within 120 days[74] and take all appropriate actions before discharging debts.[75] However, in fiscal year 2017, we found that HUD did not always follow applicable requirements for establishing and collecting debts for its Housing Choice Voucher Program. Additionally, a separate program audit[76] identified similar weaknesses in the area of debt forgiveness and termination. In fiscal year 2018, these conditions still existed because PIH had not yet implemented necessary changes to its debt collection functions and OCFO's efforts to coordinate with program offices faltered. Therefore, HUD's noncompliance with DCIA as amended continues, and as a result, it is unable to recoup money due HUD that could be used to serve the public.

HUD Did Not Always Follow Applicable Requirements When Establishing and Collecting Housing Choice Voucher Debts

In fiscal year 2017, we found that PIH did not perform the proper procedures necessary to establish legally enforceable repayments or refer delinquent debts to the OCFO debt collection claims officer (DCCO). We identified 32 program debts owed by PHAs totaling $27 million that were not under a repayment agreement and had debt identification dates between July 2003 and August 2016. There were six additional debts totaling $2.7 million that were under a repayment agreement but had no payments applied to the debt and were in delinquent status. All 38 of these debts were aged more than 120 days from the debt identification date but had not been referred to Treasury or the U.S. Department of Justice for collection. Further, they had not been evaluated by the OCFO DCCO to determine whether they were still collectable or should be written off.

In fiscal year 2018, most of these HCVP debts were still not serviced properly. Of the 32 HCVP delinquent debts without a repayment agreement, 24 remained without repayment agreements in fiscal year 2018, totaling $19.4 million. Further, OCFO had not evaluated the debts for collectability or writeoff. Without executing repayment agreements, HUD cannot lawfully

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74 Public Law 104-134—Apr. 26, 1996, 110 STAT. 1321 Sec. 31001. Debt Collection Improvement Act of 1996. (6) Any Federal agency that is owed by a person a past due, legally enforceable nontax debt that is over 180 days delinquent, including nontax debt administered by a third party acting as an agent for the Federal Government, shall notify the Secretary of the Treasury of all such nontax debts for purposes of administrative offset under this subsection. (Note: Effective May 9, 2014 agencies were required to transfer debts for administrative offset after 120 days in accordance with the DATA Act [Digital Accountability and Transparency Act of 2014]).

75 Public Law 104-134—Apr. 26, 1996, 110 STAT. 1321 Sec. 31001. Debt Collection Improvement Act of 1996, 31 U.S.C. 3711-(g)(9). Before discharging any delinquent debt owed to any executive, judicial, or legislative agency, the head of such agency shall take all appropriate steps to collect such debt, including (as applicable)—administrative offset, tax refund offset, Federal salary offset, referral to private collection contractors, referral to agencies operating a debt collection center, reporting delinquencies to credit reporting bureaus, garnishing the wages of delinquent debtors, and litigation or foreclosure.

76 Audit Report 2017-LA-0005, HUD Did Not Always Follow Applicable Requirements When Forgiving Debts and Terminating Debt Collections

collect on outstanding debts and pursue mandated collection actions on delinquencies, and HUD is unable to recoup funds due HUD that could be used to serve the public. Further, without evaluation, HUD cannot ensure that its accounts receivable balance on its financial statements represents valid receivables.

To address shortcomings in its debt collection process, PIH determined that changes in how it managed debt collection functions were necessary. Previously, field offices were responsible for HCVP debt collection and monitoring. This process resulted in poor record keeping and inconsistent debt collection and referral efforts. In August 2018, this responsibility was moved from field offices across the country to one division (PIH QAD), which allowed for more independent oversight of the function. PIH reported that this independence was a critical change component to addressing the OIG's recommendations and complying with DCIA. We agree that this move to consolidate and standardize debt collection is essential to consistent and compliant debt collection. Although PIH made this change in August 2018, it was not able to formally resolve our related recommendations before the fiscal year ended; therefore, related recommendations remained open at fiscal yearend.

OCFO's Efforts To Coordinate With Program Offices Faltered

In audit report 2018-FO-004[77] and audit report 2017-LA-0005,[78] we reported that HUD OCFO needed to strengthen its controls to ensure compliance with DCIA. While OCFO attempted to implement controls in this area, its efforts to coordinate with program offices faltered. On March 30, 2018, OCFO sent a memorandum to HUD's general deputy assistant secretaries requesting a listing of all program action officials. It planned to use this listing to provide training and perform quarterly reconciliations of its debt listing with program offices. However, it did not hear back from any of the general deputy assistant secretaries and did not follow up on its request. Without a listing of all of HUD's action officials, OCFO was unable to determine whether its listing of debts was complete and accurate. Without a complete and accurate listing of debts, OCFO cannot begin to fully monitor any aspect of debt collection. OCFO should have prioritized following up with program offices to obtain this critical and foundational information. Without it, OCFO cannot reasonably ensure that it is managing all of HUD's debts in compliance with DCIA.

Conclusion

In fiscal year 2017, we found that HUD did not always follow applicable requirements for establishing and collecting debts for HCVP. Additionally, a separate program audit identified similar weaknesses in the area of debt forgiveness and termination. In fiscal year 2018, these conditions still existed because PIH had not yet implemented necessary changes to its debt collection functions and OCFO's efforts to coordinate with program offices faltered. As a result, HUD was unable to recoup funds due HUD that could be used to serve the public.

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[77] Audit Report 2018-FO-0004, Additional Details To Supplement Our Fiscal Years 2017 and 2016 (Restated) U.S Department of Housing and Urban Development Financial Statement Audit

[78] Audit Report 2017-LA-0005, HUD Did Not Always Follow Applicable Requirements When Forgiving Debts and Terminating Debt Collections

Recommendations

OCFO and PIH agreed with prior-year recommendations made in audit reports 2018-FO-0004 and 2017-LA-0005 and are working to implement corrective actions. The status of recommendations made in audit report 2018-FO-0004 are in the Followup on Prior Audits section of this report. We are not making any new recommendations in this report.

Finding 9: HUD Did Not Comply With the Federal Credit Reform Act

HUD did not perform annual technical reestimates for the Emergency Homeowners' Loan Program (EHLP) as required by the Federal Credit Reform Act. HUD stated that a decision was made in collaboration with OMB to not perform reestimates for EHLP; however, HUD could not provide documentation of the decision. As a result, the allowance for subsidy account is at risk of misstatement.

HUD Did Not Perform Annual Technical Reestimates for the EHLP

HUD did not comply with the requirements of the Federal Credit Reform Act when it did not perform annual technical reestimates. OMB Circular A-11, section 185, provides implementation guidance for the Federal Credit Reform Act and states that agencies are required to reestimate the subsidy cost throughout the life of each cohort of direct loans to account for differences between original assumptions of cash flow and actual cash flow or revised assumptions about future cash flow. Technical reestimates, made to adjust for revised assumptions about loan performance, must be made after the close of each fiscal year, unless an alternative plan has been approved by OMB. According to Office of Housing officials, HUD did not perform annual technical reestimates for EHLP because HUD had consulted with OMB and decided that performing reestimates was not a priority for this program because of low activity. However, HUD was not able to provide documentation to support this decision, stating that the decision may have been through verbal communication.

While OMB Circular A-11 does not prescribe a format for a plan that deviates from requirements, GAO's Standards for Internal Control in the Federal Government, the Green Book, requires agencies to have control activities in place to help ensure that agency objectives are met. Control activities include proper authorization and appropriate documentation and access to that documentation. Management is responsible for documenting internal control, all transactions, and other significant events in a manner that allows the documentation to be readily available for examination. As a result, EHLP's allowance for subsidy account may be misstated; therefore, the EHLP loans receivable balance may be misstated.

Conclusion

HUD did not comply with requirements of the Federal Credit Reform Act and could not provide documentation to support its decision to forego performing annual technical reestimates for EHLP. The lack of annual technical reestimates means that the allowance for subsidy account for EHLP may be misstated and as a result, EHLP's loans receivable balance may also be misstated.

Recommendations

We recommend that the Office of Housing's Deputy Assistant Secretary for Finance and Budget

9A. Develop technical reestimates for the EHLP direct loan portfolio annually in accordance with the requirements in OMB Circular A-11, section 185, and submit the reestimates to OCFO and ARC for recording.

Finding 10: HUD Potentially Violated the Antideficiency Act

The OCFO Appropriations Law Division (ALD) had 10 ongoing investigations related to possible ADA violations. ALD had not maintained adequate documentation to support the status of its ongoing investigations. As a result, we were unable to assess the potential impact to HUD's financial statements from the potential ADA violations and compliance with the law.

The OCFO Appropriations Law Division Was Investigating 10 Potential ADA Violations

OCFO specified 10 ongoing investigations, 2 of which were opened in fiscal year 2017 and the rest opened during fiscal year 2018. One case was a referral from OIG related to expenditures exceeding grant round obligations for grantees receiving Disaster Relief Appropriations Act, 2013, funds.[79] Other open cases related to (1) appropriations act provisions related to performance awards prohibitions, (2) insufficient funds to obligate and pay for shared service provider invoices, (3) furniture and office redecoration spending limitations exceeded without prior congressional notification, and (4) subsidy contracts with insufficient funds available to pay for the duration of the contract. All open cases are under investigation and pending final determinations.

We attempted to review these cases to determine the scope and extent of OCFO's investigation and compliance with reporting requirements and potential financial statement implications. However, we were unable to do so because OCFO had not prepared case file documentation and did not foresee having the ability to do so and have it available for inspection in a timely fashion. As a result, we were not able to assess compliance with the ADA and the potential financial statement impact from these ongoing investigations.

Conclusion

OCFO ALD had 10 open ongoing investigations of potential ADA violations as of September 30, 2018. OCFO ALD was unable to provide documentation on the current status of each case. Therefore, we were unable to assess the impact of potential noncompliance with laws and regulations on HUD's financial statements impact from these ongoing investigations.

Recommendations

We recommend that the Chief Financial Officer

10A. Implement a process to ensure that ongoing ADA violation investigations are properly documented as the investigation progresses to enable timely review of open cases.

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[79] Audit Memorandum 2018-FW-0802, Interim Report - Potential Antideficiency Act and Generally Accepted Accounting Principle Violations Occurred With Disaster Relief Appropriation Act, 2013, Funds, issued May 15, 2018

Finding 11: HUD Did Not Comply With the Improper Payments Elimination and Recovery Act of 2010

HUD OIG's Improper Payments Elimination and Recovery Act (IPERA) audit[80] found that HUD did not comply with IPERA, as amended, in fiscal year 2017 because it did not conduct its annual risk assessment and failed to publish improper payment estimates in accordance with OMB guidance. This is the fifth consecutive year that HUD has not complied with IPERA. This failure to comply occurred because HUD's remediation plans that were intended to address many of the IPERA compliance issues were not in place at the end of fiscal year 2017. Therefore, HUD's programs continued to be vulnerable to the adverse effects of improper payments.

HUD Did Not Perform Risk Assessments in Accordance With OMB Guidance

For the past 2 years, we have cited HUD for noncompliance with OMB's annual risk assessment requirement. In our most recent audit conducted in fiscal year 2018, we again found HUD noncompliant with the requirement. Specifically, we noted that HUD had not assessed the risk of improper payments for 14 HUD programs. As a result, HUD likely missed opportunities to identify programs vulnerable to significant improper payments, which could lead to a waste of government resources.

HUD Did Not Report Improper Payment Estimates in Accordance With OMB Guidance

HUD did not comply with IPERA because it failed to report in its AFR the $837 million improper payment estimate for its single-family insurance claims program. HUD mistakenly omitted this information when it finalized its fiscal year 2017 AFR. This deficiency occurred because HUD did not have effective control in managing its AFR processing risks.

With respect to HUD's Rental Housing Assistance Programs, HUD did not comply with IPERA because the amount of the RHAP improper payment estimate reported in its fiscal year 2017 AFR was not based on a statistically valid estimate as required by OMB Circular A-123, appendix C. HUD disclosed this information in its fiscal year 2017 AFR, which states that "the disclosed amounts for RHAP do not provide a statistically valid estimate of improper payments."[81]

Conclusion

Fiscal year 2017 marked the fifth consecutive year in which HUD had not complied with IPERA. As a result of its noncompliance, HUD's limited program funds could not be maximized to benefit its intended recipients. Although we recognize HUD's ongoing efforts and plans to remediate many of the improper payment-related issues, if HUD does not address its noncompliance, it will continue to miss opportunities to prevent, identify, and recover improper payments.

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80 Audit Report 2018-FO-0006, Compliance With the Improper Payments Elimination and Recovery Act, issued May 15, 2018

81 HUD fiscal year 2017 AFR, page 178

Recommendations

Recommendations were included in a separate OIG audit report. Therefore, no recommendations are reported here.

Other Matter

Significant Amounts of Emergency Home Loan Program Funds Remained but Were Unavailable

We reported last year that the program account for EHLP had $329.4 million in unapportioned, no-year funds remaining and recommended that HUD seek authority from Congress to return the funds to Treasury because they could no longer be used for the purposes of the program.[82] As of September 30, 2018, these funds remained in the EHLP program account because the process to return the funds to Treasury could not be completed under existing authority.

Significant Amounts of Unapportioned Funds Remained in the EHLP Program Account

The Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203, states that no emergency mortgage relief payments were to be made after September 30, 2011, unless such payments were made with respect to a borrower's receiving the benefit of emergency relief payments made on such date, establishing an obligation deadline of September 30, 2011, for EHLP funds. As a result, any remaining unapportioned funds in the EHLP program account can no longer be used to make emergency mortgage relief payments.

During fiscal year 2018, HUD started the process to return the $329.4 million in unapportioned funds remaining in the EHLP program account to Treasury; however, as of September 30, 2018, the process had not been completed. HUD staff informed us that for each transaction impacting the General Fund of the U.S. Government, it must provide Treasury with a citation identifying the requisite statutory authority. The return of unused, unapportioned funds was not authorized in Public Law 111-203, and Congress did not include a rescission for EHLP in HUD's fiscal year 2018 appropriations. HUD staff was able to identify other existing authority, 31 U.S.C. (United States Code)1555, "Closing of appropriation accounts available for indefinite periods," which may be used to return funds when an account is being closed. Under this authority, the EHLP program account may be closed when it has been 2 years since the final disbursement and the Secretary acknowledges that this closing process is permanent and irreversible. Since the most recent disbursement from the EHLP program account occurred in fiscal year 2016, HUD was not able to return the $329.4 million in unapportioned funds to Treasury during fiscal year 2018, and it remained in the EHLP program account as of September 30, 2018. HUD expects to complete the process of returning the funds to Treasury during fiscal year 2019.

Conclusion

HUD did not use all of the funding provided for EHLP, and the remaining funds cannot be used to make new loans or emergency mortgage relief payments. As a result, $329.4 million in

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[82] Audit Report 2018-FO-0004, Additional Details To Supplement Our Fiscal Years 2017 and 2016 (Restated) U.S. Department of Housing and Urban Development Financial Statement Audit

unapportioned funds will remain on HUD's financial statements until they are returned to Treasury.

Recommendations

Prior-year recommendations regarding this matter remained open and can be referred to in the Followup on Prior Audits section of this report. We have no new recommendations in this report.

Scope and Methodology

We are required by the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994 and implemented by OMB Bulletin 19-01, Audit Requirements for Federal Financial Statements, to audit HUD's principal financial statements, which consist of the consolidated balance sheets as of September 30, 2018 and 2017 (restated); the related consolidated statements of net cost, changes in net position, and combined statement of budgetary resources for the fiscal years then ended; and the related notes to the financial statements.

We considered internal controls over financial reporting by obtaining an understanding of the design of HUD's internal controls, determined whether these internal controls had been placed into operation, assessed control risk, and performed tests of controls to determine our auditing procedures for the purpose of expressing an opinion on the principal financial statements. We also evaluated the internal controls in place at HUD's FSSP, ARC, by reviewing its Statement on Standards for Attestation Engagements (SSAE) 18 report for the current period to determine whether the FSSP's internal controls could be relied upon. We tested compliance with selected provisions of applicable laws, regulations, contracts, and grant agreements that may materially affect the consolidated principal financial statements. The tests performed were not to provide assurance on these internal controls, and, accordingly, we do not provide assurance or an opinion on such controls.

We did not evaluate the internal controls relevant to operating objectives as broadly defined by FMFIA. We limited our internal controls testing to those controls that are material in relation to HUD's financial statements. Because of limitations inherent in any internal control structure, misstatements may occur and not be detected. We also caution that projection of any evaluation of the structure to future periods is subject to the risk that controls may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

Our consideration of the internal controls over financial reporting would not necessarily disclose all matters in the internal controls over financial reporting that might be significant deficiencies. We noted certain matters in the internal control structure and its operation that we considered to be significant deficiencies under OMB Bulletin 19-01.

We considered HUD's internal controls over required supplementary stewardship information reported in HUD's fiscal year 2018 AFR by obtaining an understanding of the design of HUD's internal controls, determined whether these internal controls had been placed into operation, assessed control risk, and performed limited testing procedures as required by the American Institute of Certified Public Accountants and U.S. Auditing Standards, AU-C, Section 730, Required Supplementary Information. The tests performed were not to provide assurance on these internal controls, and, accordingly, we do not provide assurance or an opinion on such controls.

With respect to internal controls related to performance measures to be reported in management's discussion and analysis and HUD's fiscal year 2018 AFR, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions. We performed limited testing procedures as required by AU-C, Section 730, Required Supplementary Information, and OMB Bulletin 19-01, Audit Requirements for Federal Financial Statements. Our procedures were not designed to provide assurance on internal controls over reported performance measures, and, accordingly, we do not provide an opinion on such controls.

To fulfill these responsibilities, we

- Examined, on a test basis, evidence supporting the amounts and disclosures in the consolidated principal financial statements.
- Assessed the accounting principles used and the significant estimates made by management.
- Evaluated the overall presentation of the consolidated principal financial statements.
- Obtained an understanding of internal controls over financial reporting (including safeguarding assets) and compliance with laws and regulations (including the execution of transactions in accordance with budget authority).
- Tested and evaluated the design and operating effectiveness of relevant internal controls over significant cycles, classes of transactions, and account balances.
- Tested HUD's compliance with certain provisions of laws and regulations; governmentwide policies, noncompliance with which could have a direct and material effect on the determination of financial statement amounts; and certain other laws and regulations specified in OMB Bulletin 19-01, including the requirements referred to in FMFIA.
- Considered compliance with the process required by FMFIA for evaluating and reporting on internal controls and accounting systems.
- Performed other procedures we considered necessary in the circumstances.

Under standards issued by the American Institute of Certified Public Accountants, 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. 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.

A material weakness is a deficiency or combination of deficiencies in internal controls, such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented or detected and corrected on a timely basis.

Our work was performed in accordance with generally accepted government auditing standards and OMB Bulletin 19-01. 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 objective.

Followup on Prior Audits

Recommendations from prior-year reports on HUD's financial statements that have not been fully implemented based on the status reported in the Audit Resolution and Corrective Action Tracking System as of October 1, 2018, are included in the list below. Specifically, we identified 93 unimplemented recommendations from prior-year reports, dating back to the audit of the fiscal years 2010 and 2009 financial statements. Each of these open recommendations and its status is shown below.

We also noted that as of October 29, 2018, management had established action plans for 80 of 93 unimplemented recommendations referenced above, of which 56, or 70 percent, were past agreed-upon dates for final action. HUD did not have established action plans for the 13 additional recommendations.

Followup on prior audits			
Audit rec #	**Program office**	**Open recommendations**	**Final action target date**
Additional Details To Supplement Our Fiscal Years 2017 and 2016 (Restated) U.S. Department of Housing and Urban Development Financial Statement Audit, 2018-FO-0004, November 15, 2017			
2018-FO-0004-001-A	OCFO	Implement a repeatable and sustainable process to prepare timely and accurate quarterly financial statement notes, including third and fourth quarter notes within the OMB required timeframe.	12/15/2018
2018-FO-0004-002-A	OCFO	Work with PIH to develop and implement a consistent and reasonable methodology for determining the PIH prepayment that (1) allows for timely recording of financial events, (2) complies with GAAP, and (3) provides an adequate audit trail until the cash management process is automated.	1/12/2019
2018-FO-0004-002-B	OCFO	Develop and implement procedures to ensure that the methodology is reevaluated by PIH and OCFO annually and any changes do not compromise (1) the audit trial, (2) compliance with GAAP, or (3) the accuracy of the balance.	2/19/2019
2018-FO-0004-002-F	PIH	Work with OCFO to develop a consistent and reasonable methodology for determining the PIH prepayment, which (1) allows for timely recording of financial events, (2) complies with GAAP, and (3) provides an adequate audit trail until the cash management process is automated.	10/31/2018

2018-FO-0004-005-A	OCFO	Implement an information system or system application that can produce HUD’s consolidated financial statement notes accurately and in a timely manner.	11/30/2018
2018-FO-0004-006-A	OCFO	Establish and implement policies and procedures that require identification and performance of complementary controls and periodic evaluation of established complementary controls to ensure that they continue to address financial and operational risks and document, assign, and communicate user complementary controls roles and responsibilities.	6/30/2018
2018-FO-0004-007-E	OCPO	Ensure that originating base IAAs [interagency agreements] and modifications are maintained in HUD’s procurement system of record, PRISM, including manual documentation and records from HIAMS [HUD Integrated Acquisition Management System].	N/A
2018-FO-0004-008-A	OCFO	Improve controls to ensure that the OOR process is successful. This includes but is not limited to the following: (1) providing clarity on what constitutes a reasonable justification for retaining obligations marked for review during the OOR and (2) ensuring that a reasonable amount of time is provided for program offices to adequately complete the markup review phase of the OOR.	10/15/2018
2018-FO-0004-008-B	OCFO	Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $212,447 in 46 administrative obligations and 1 program obligation totaling $135,956 marked for deobligation as of September 30, 2017.	6/30/2018
2018-FO-0004-008-C	CPD	Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $11,463,971 in 189 program obligations and $13,640 in 10 administrative obligations marked for deobligation as of September 30, 2017.	3/12/2019
2018-FO-0004-008-D	CPD	Review the 1,110 identified inactive retained obligations with remaining balances totaling $229,327,332 and close out and deobligate amounts tied to obligations that are no longer valid or needed.	3/12/2019
2018-FO-0004-008-E	CPD	Close out and deobligate the remaining balances on 2,741 expired homeless assistance contracts of $159,437,069.	11/10/2018

2018-FO-0004-008-F	Housing	Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $42,491,202 in 581 administrative obligations and $2,932,320 in 12 program obligations marked for deobligation as of September 30, 2017.	9/30/2018
2018-FO-0004-008-G	Housing	Review the 84 identified inactive retained obligations with remaining balances totaling $56,435,559 and close out and deobligate amounts tied to obligations that are no longer valid or needed.	9/30/2018
2018-FO-0004-008-H	Housing	Review and if necessary deobligate the 40 and 30 expired or inactive Section 236 and Section 202-811 projects totaling $17,416,572 and $86,715,301, respectively.	9/15/2018
2018-FO-0004-008-J	AO	Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $2,266,017 in 100 administrative obligations marked for deobligation as of September 30, 2017.	6/8/2018
2018-FO-0004-008-L	FHEO	Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $559,569 in 53 administrative and $641,110 in 9 program obligations marked for deobligation as of September 30, 2017.	1/4/2019
2018-FO-0004-008-M	FHEO	Review the seven identified retained inactive obligations with remaining balances totaling $143,344 and close out and deobligate amounts tied to obligations that are no longer valid or needed.	12/7/2018
2018-FO-0004-008-N	PD&R	Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $279,282 in 11 administrative obligations marked for deobligation as of September 30, 2017.	10/31/2018
2018-FO-0004-008-O	OCIO	Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $264,476 in 108 administrative obligations marked for deobligation as of September 30, 2017.	2/7/2019
2018-FO-0004-008-P	CHCO	Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $257,102 in 55 administrative obligations marked for deobligation as of September 30, 2017.	10/24/2018
2018-FO-0004-008-Q	OGC	Deobligate all obligations marked for deobligation during the departmentwide OOR, including as much as $174,132 in 160 administrative obligations marked for deobligation as of September 30, 2017.	9/29/2018

2018-FO-0004-008-S	Ginnie Mae	Deobligate all obligations marked for deobligation during Ginnie Mae's open obligation review, including as much as $34,814,053 in eight contract obligations marked for deobligation.	6/30/2018
2018-FO-0004-011-A	PIH	For all 32 debts not under repayment agreement, (1) send demand letters for any debts for which a demand letter has not been sent and (2) aggressively work with the PHAs to determine appropriate repayment agreement terms.	10/31/2018
2018-FO-0004-011-B	PIH	Establish procedures to ensure that the debt file is sent to the OCFO DCCO for claim establishment if initial collection attempts prove unsuccessful.	10/31/2018
2018-FO-0004-011-C	PIH	Establish procedures to routinely send all debts (delinquent or not) to OCFO for evaluation as required by the debt collection handbook.	12/31/2018
2018-FO-0004-011-D	PIH	Finalize the repayment agreement procedures and implement training to ensure that all of PIH is aware of the procedures. The repayment agreement procedures should ensure that PIH follows HUD's debt collection handbook.	12/31/2018
2018-FO-0004-011-E	OCFO	Work with PIH to determine which debts should be transferred to the Departments of Treasury or Justice and which debts should be written off. The Deputy CFO should ensure that proper documentation is maintained to support a decision for writeoff.	4/13/2019
2018-FO-0004-013-A	OCFO	Determine the amount of additional funds needed to cover the remaining administrative costs and any possible upward adjustment of current obligations and seek authority from Congress to return up to $329,370,982 of the unapportioned authority remaining in the EHLP program account that is not needed.	10/15/2018
Additional Details To Supplement Our Fiscal Years 2016 and 2015 (Restated) U.S. Department of Housing and Urban Development Financial Statement Audit, 2017-FO-0003, November 15, 2016			
2017-FO-0003-002-A	OCFO	Continue working with ARC and complete the reconciliation and cleanup efforts for balances related to HUD's loan guarantee programs.	N/A
2017-FO-0003-002-C	OCFO	Work with the Office of the Chief Administration Officer to establish control activities (that is, procedures) to completely and accurately record internal use software, leasehold improvement, and	4/15/2019

		property acquisition transactions and enable compliant financial reporting.	
2017-FO-0003-002-E	OCFO	Work with the OCFO to establish controls that ensure the timely communication of internal use and commercial-off-the-shelf software license acquisition activity and data.	04/15/2019
2017-FO-0003-002-F	OCFO	Work with OCFO to develop control activities that address risks related leasehold improvement and property acquisition data completeness and accuracy.	4/15/2019
2017-FO-0003-003-B	OCFO	Continue the subledger reconciliation project and complete it in a timely manner, communicate results to top key stakeholders, and complete necessary adjustments or restatements (if applicable).	N/A
2017-FO-0003-003-C	OCFO	Perform a root cause analysis to identify potential control gaps and ineffective controls in the review of subledger balances to the general ledger.	N/A
2017-FO-0003-003-D	OCFO	Communicate the impact of system limitations that contributed to unreconciled balances to relevant management and design and implement effective controls that address relevant risks.	N/A
2017-FO-0003-006-A	OCFO	Establish a framework for financial policy development and review of policy and procedures that defines roles and responsibilities and provides reasonable assurance regarding the effectiveness of related controls.	N/A
2017-FO-0003-008-A	CPD	Close out and deobligate the remaining balances on 3,121 expired homeless assistance contracts of $151,719,152. Further, deobligate $10,996,784 in 234 program obligations marked for deobligation during the departmentwide open obligations review.	11/10/2018
2017-FO-0003-008-E	CPD	Research grants with no drawdown activity and if a bonafide need no longer exists, close out and deobligate remaining balances on the 16 grants with no drawdown activity totaling $6,966,585.	08/15/2017
2017-FO-0003-008-F	Housing	Deobligate all obligations marked for deobligation during the departmentwide open obligations review, including as much as $18,290,686 in 307 administrative obligations and $3,420,032 in 202 program obligations marked for deobligation as of September 30, 2016.	06/05/2017
2017-FO-0003-008-G	Housing	Review and if necessary deobligate the 785 expired or inactive Section 235-236, Section 202-811, and	03/22/2018

		Project Based Section 8 projects totaling $22,075,052, $12,261,389, and $384,125, respectively.	
2017-FO-0003-008-H	OCFO	Deobligate the $83,501 in 124 administrative obligations marked for deobligation during the departmentwide open obligations review.	01/19/2018
2017-FO-0003-008-K	FHEO	Deobligate all obligations marked for deobligation during the departmentwide open obligations review, including as much as $384,703 in 27 administrative obligations and $234,619 in 6 program obligations marked for deobligation as of September 30, 2016.	12/29/2017
2017-FO-0003-008-P	Ginnie Mae	Review the contracts totaling $72.8 million to determine validity and if no longer needed, forward to HUD's procurement office for closure and deobligation.	09/30/2017
2017-FO-0003-008-Q	Ginnie Mae	Record the deobligations provided by OCPO totaling as much as $86.4 million for the contracts identified during our review. Additionally, Ginnie Mae should deobligate the $587,505 in three administrative obligations marked for deobligation during the departmentwide open obligations review	09/30/2017
Additional Details To Supplement Our Fiscal Years 2015 and 2014 (Restated) U.S. Department of Housing and Urban Development Financial Statement Audit, 2016-FO-0003, November 18, 2015			
2016-FO-0003-002-A	OCFO	Evaluate the IHBG investment process and implement a proper accounting treatment in accordance with Federal GAAP.	12/30/2017
2016-FO-0003-002-B	OCFO	Work with the Office of Native American Programs to calculate the amounts advanced to grantees and restate HUD's financial statements to recognize the prepayments on the financial statements.	12/30/2017
2016-FO-0003-002-C	OCFO	Develop standard operating procedures for routinely obtaining information on grantee investment activity and accurately reporting amounts in HUD's general ledger and financial statements.	12/30/2017
2016-FO-0003-002-D	PIH	Establish a process to track the amount HUD owes to PHAs to cover prepayment shortages and provide the information to OCFO so that it can be properly recognized as accounts payable.	N/A
2016-FO-0003-002-E	PIH	Develop a tracking function for the payments advanced to IHBG recipients to facilitate financial reporting and monitoring compliance with grant time restrictions.	12/30/2017

2016-FO-0003-006-A	OCFO	Evaluate the weaknesses identified by NAPA [National Academy of Public Administration], as well as OCFO's disagreement with those weaknesses and recommendations, and identify what corrective actions will be taken and when those actions will be taken.	7/31/2018
2016-FO-0003-006-B	OCFO	Develop a process to ensure that issues and recommendations from all evaluations and audits, including those performed by third parties like NAPA, are adequately documented and tracked and properly evaluated by senior management to ensure that HUD's FMFIA structure remains compliant. HUD should also ensure that corrective actions are agreed upon and responsibility for implementing corrective actions is appropriately delegated.	N/A
2016-FO-0003-006-C	OCFO	Develop procedures to provide oversight of OCPO procurement activities to ensure that those with financial accounting and reporting impact are properly captured and reflected in HUD's financial statements.	N/A
2016-FO-0003-006-D	OCFO	Review projects and acquisitions to determine whether the proper accounting treatment was applied and determine whether corrections to HUD's financial statements are needed.	N/A
2016-FO-0003-006-E	OCFO	Contact all other HUD program offices to determine whether any other programs authorize or are aware of grantees holding funds in advance of their immediate disbursement needs and determine financial statement impact on and compliance with Treasury cash management requirements of any found.	N/A
2016-FO-0003-006-F	OCFO	Distribute the workload among available accountants when staff is unavailable to ensure that all cash reconciliations are performed in a timely manner.	8/31/2016
2016-FO-0003-006-J	OCFO	Revise policies and procedures to ensure that MCRs are routinely monitored and completed for all program areas and establish a timeframe for completion of the MCR reports. Further, HUD should ensure that an escalation process is included to address untimely completion of the MCR process.	3/17/2017
2016-FO-0003-008-A	CPD	Close out and deobligate the remaining balances on 2,308 expired homeless assistance contracts of $104,347,996. HUD should also deobligate $3,602,342 in 102 program obligations marked for deobligation during the departmentwide open obligations review. Lastly, HUD should review the 57 obligations with remaining balances of $188,176 and	3/16/2017

		close out and deobligate amounts tied to obligations that are no longer valid or needed.	
2016-FO-0003-008-E	Housing	Deobligate all obligations marked for deobligation during the departmentwide open obligations review, including as much as $19,634,263 in 209 administrative obligations and $2,224,807 in 24 program obligations marked for deobligation as of September 30, 2015. Additionally, HUD should review the 225 obligations with remaining balances of $285,024 and close out and deobligate amounts tied to obligations that are no longer valid or needed.	3/9/2017
2016-FO-0003-008-F	Housing	Review and if necessary deobligate the 228, 477, and 29 expired or inactive project-based Section 8, Section 235-236, and Section 202-811 projects totaling $52.5 million, $36.2 million, and $1.3 million, respectively.	2/3/2017
2016-FO-0003-008-H	OCIO	Deobligate all obligations marked for deobligation during the departmentwide open obligations review, including as much as $430,942 in 44 administrative obligations and $135,957 in 2 program obligations marked for deobligation as of September 30, 2015. Additionally, HUD should review the 17 obligations with remaining balances of $1,486,191 and close out and deobligate amounts tied to obligations that are no longer valid or needed.	2/2/2017
2016-FO-0003-008-K	FHEO	Deobligate $140,165 in 41 administrative and $125,166 in 3 program obligations marked for deobligation during the departmentwide open obligations review.	12/8/2016
2016-FO-0003-008-L	EEO	Review the 20 obligations with remaining balances of $77,807 and close out and deobligate amounts tied to obligations that are no longer valid or needed.	3/22/2017
2016-FO-0003-008-O	Ginnie Mae	Deobligate the $587,198 in eight administrative obligations marked for deobligation during the departmentwide open obligations review.	3/21/2017
2016-FO-0003-013-A	PIH	Complete any outstanding validation reviews and transition back as much as $466.5 million in Housing Choice Voucher program funding from MTW PHAs and $41 million from non-MTW PHAs.	9/30/2021
Interim Report on HUD's Internal Controls Over Financial Reporting, 2015-FO-0002, December 8, 2014			

2015-FO-0002-001-A	CPD	Continue to work with CPD's IT information technology services contractor and OCFO to ensure that all three phases of the plan to bring IDIS into compliance with GAAP and applicable Federal system requirements are completed as scheduled.	1/31/2017
2015-FO-0002-006-B	CPD	Deobligate $174,168 in 5 administrative obligations and $9,920,926 in 308 program obligations marked for deobligation during the departmentwide open obligations review. Additionally, review the 72 obligations with remaining balances totaling $313,419 and close out and deobligate amounts tied to obligations that are no longer valid or needed.	10/1/2015
2015-FO-0002-006-F	Housing	Deobligate the 76 expired or inactive Sections 202 and 811 and project-based Section 8 projects totaling $3,458,166.	3/4/2016
2015-FO-0002-006-J	OCIO	Deobligate all obligations marked for deobligation during the departmentwide open obligations review, including as much as $3,561,042 in 64 administrative obligations marked for deobligation as of September 29, 2014. Additionally, review the 171 obligations with remaining balances totaling $19,730,791 and close out and deobligate amounts tied to obligations that are no longer valid or needed.	3/6/2016
2015-FO-0002-006-U	FHEO	Deobligate $5,210 in two administrative obligations and $109,500 in one program obligation marked for deobligation during the departmentwide open obligations review. Additionally, review the 17 obligations with remaining balances totaling $26,711 and close out and deobligate amounts tied to obligations that are no longer valid or needed.	12/16/2015
2015-FO-0002-007-D	OCFO	Periodically reconcile balances with OCIO subsidiary records and research and resolve any identified differences.	3/31/2016
2015-FO-0002-007-I	OCIO	Develop a subsidiary system to accumulate the capitalized cost and related depreciation expense for each software project under development or placed into production.	4/15/2019
Additional Details To Supplement Our Report on HUD's Fiscal Years 2013 and 2012 (Restated) Financial Statements, 2014-FO-0003, December 16, 2013			

2014-FO-0003-001-A	CPD	Develop and implement a detailed remediation action plan to ensure that grant management systems eliminate the FIFO methodology in its entirety. The plan should (1) explain how the budget fiscal year-TAFS [Treasury Account Fund Symbol] for each accounting transaction (project and activity setup, commitment, disbursement, etc.) will be recorded, remain constant, and be maintained, (2) reference Federal system requirements and criteria, and (3) include resources, specific remedies, and intermediate target dates necessary to bring the financial management system into substantial compliance.	9/30/2014
2014-FO-0003-001-C	OCFO	Provide oversight of CPD's system implementation or modification to ensure that Federal financial management accounting standards are embedded into the system so that the information transferred from grant management systems to HUD's core financial systems comply with these standards, are recorded in HUD's consolidated financial statements in accordance with Federal GAAP, and ensure that compliant administrative control of funds for its formula grant programs is established.	10/30/2015
2014-FO-0003-002-A	PIH	Transition the PHA NRA [Net Restricted Assets] excess funds, which are as much as $643.6 million as of June 30, 2013, to HUD's control as soon as possible to safeguard the program resources.	12/31/2057[83]
2014-FO-0003-002-C	PIH	Implement a cost-effective method for automating the cash management process to include an electronic interface of transactions to the standard general ledger.	N/A
2014-FO-0003-002-E	OCFO	Review the cash management process to identify all financial events to be recognized in accordance with GAAP. Establish procedures to account for the cash management activity in a timely manner in compliance with GAAP.	4/8/2015
2014-FO-0003-002-G	OCFO	Ensure that PIH's automation of its cash management process complies with Federal financial management requirements.	12/31/2015

[83] Recommendation is under repayment.

2014-FO-0003-003-A	OCFO	Design and Implement a loan guarantee system that complies with the Guaranteed Loan System Requirements. Ensure that the implemented loan guarantee system should be integrated with HUD's financial management systems and be included in its financial management system plans.	12/31/2015
2014-FO-0003-004-G	OCFO	Establish an appropriate accounting and financial reporting governance structure within OCFO with the appropriate level of accounting, experience, and training to support the size and complexity of HUD's and its component entities' financial reporting requirements.	3/11/2015
2014-FO-0003-006-C	OCFO	Enforce already existing internal control procedures to ensure proper supervision over accounting for Section 8 FAF [Financing Adjustment Factor] receivables.	10/1/2014
2014-FO-0003-006-D	OCFO	Perform a thorough analysis of outstanding FAF receivables and fiscal year 2013 collections to ensure that the receivables accurately represent the amounts owed to HUD, including but not limited to positive confirmations of outstanding receivable balances with the trustees.	3/4/2015
2014-FO-0003-008-B	CPD	Complete the closeout of any remaining CDBG-DR [Community Development Block Grant Disaster Recovery] and HPRP [Homelessness Prevention and Rapid Rehousing Program] grants and forward all grant closeout agreement certifications to OCFO for recapture.	9/30/2014
2014-FO-0003-008-C	CPD	Deobligate $14,425,629 tied to 238 program obligations marked for deobligation during the departmentwide unliquidated obligations review. Additionally, OCFO should review the 93 obligations with remaining balances totaling $316,935 and close out and deobligate amounts tied to obligations that are no longer valid.	4/3/2015
2014-FO-0003-008-E	Housing	Research and deobligate at least $9.3 million tied to the 115 inactive and/or expired Section 202/811 funding lines.	4/2/2015
2014-FO-0003-008-F	Housing	Review and deobligate at least $26 million tied to 215 inactive and/or expired Section 8 obligations.	4/2/2015

2014-FO-0003-008-M	OCFO	Design and implement a policy to ensure that reconciliations between the subsidiary ledgers (supporting records) and the obligation balances in the general ledger (controlling accounts) are periodically performed for all HUD appropriations. The policy should also address the follow-up and clearance of identified differences and the responsibilities for the preparers and reviewers.	4/1/2015
2014-FO-0003-008-O	OCIO	Deobligate $7,263,662 tied to 178 administrative obligations marked for deobligation during the departmentwide unliquidated obligations review.	2/13/2015
Additional Details To Supplement Our Report on HUD's Fiscal Years 2012 and 2011 Financial Statements, 2013-FO-0003, November 15, 2012			
2013-FO-0003-003-C	OCFO	Develop and implement formal financial management policies and procedures to require an annual evaluation by OCFO and applicable program offices of all allowance for loss rates and other significant estimates currently in use to ensure appropriateness.	11/29/2013
2013-FO-0003-006-B	CPD	Review the 270 obligations with remaining balances totaling $432,147 and close out and deobligate amounts tied to obligations that are no longer valid or needed.	9/30/2014
Additional Details To Supplement Our Report on HUD's Fiscal Years 2010 and 2009 Financial Statements, 2011-FO-0003, November 15, 2010			
2011-FO-0003-001-D	CPD	Include as part of the annual CAPER [consolidated annual performance and evaluation report], a reconciliation of HUD's grant management system, IDIS, to grantee financial accounting records on an individual annual grant basis, not cumulatively, for each annual grant awarded to the grantee.	6/15/2015
2011-FO-0003-002-C	OCFO	Review the 510 obligations which were not distributed to the program offices during the open obligations review and deobligate amounts tied to closed or inactive projects, including the $27.5 million we identified during our review as expired or inactive.	10/31/2011

Appendixes

Appendix A

Schedule of Funds To Be Put to Better Use

Recommendation number	Funds to be put to better use[1]
5E	$ 7,579,669
5F	43,005,703
5G	56,746,431
5H	4,310,534
5I	588,694
5J	78,069
5K	168,198
5L	110,224
5M	574,511
5N	106,962
5O	60,395
5P	54,909
Totals	**236,326,397**

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.

Appendix B

Schedule of Recommended Deobligations

Invalid obligations identified by HUD but not deobligated as of September 30, 2018[84]						
Program office	Administrative obligations		Program obligations		Total	
	#	$	#	$	#	$
Housing	735	51,396,319	68	5,350,112	803	56,746,431
CPD	9	62,183	187	7,517,486	196	7,579,669
PIH	12	588,694			12	588,694
OCHCHO	79	574,511			79	574,511
FHEO	29	168,195			29	168,195
ODEEO	30	106,962			30	106,962
PD&R	13	54,909			13	54,909
Total[85]	907	52,951,773	255	12,867,598	1,162	**65,819,371**

OCHCO – Office of the Chief Human Capital Officer
FHEO – Office of Fair Housing and Equal Opportunity
DEEO – Office of Departmental Equal Employment Opportunity
PD&R – Office of Policy Development and Research

Obligations marked retained, inactive[86]		
Program office	**#**	**$**
Community Planning and Development	473	43,005,703
Office of Housing	65	4,310,534
Office of Fair Housing Equal Opportunity	5	110,224
Office of Public and Indian Housing	3	78,069
Office of Lead Hazard Control and Healthy Homes	1	60,395
Total	**547**	**47,564,925**

[84] HUD's departmentwide unliquidated obligation review
[85] Differences due to rounding
[86] No activity for 2 years or more

Appendix C

Auditee Comments and OIG's Evaluation

Ref to OIG Evaluation	Auditee Comments

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

November 6, 2018

MEMORANDUM FOR: Thomas R. McEnanly, Director of Financial Audits Division, HUD, GAH

FROM: George Tomchick, III, Deputy Chief Financial Officer, HUD, F

SUBJECT: Response to Fiscal Year 2018 Financial Statement Audit – Transmittal of Draft Fiscal Year 2018 Independent Additional Details on HUD's Fiscal Year 2018 and 2017 Consolidated Financial Statements

Comment 1

HUD is committed to fulfilling its mission to create strong, sustainable, inclusive communities and quality affordable homes for American families and individuals. The work of HUD's Office of Inspector General (OIG) helps to ensure that HUD programs and employees work to successfully accomplish these goals.

HUD agrees that it cannot continue to operate in the absence of a clean audit opinion, and we are committed to making the business process changes necessary to resolve the longstanding material weaknesses in internal controls. We look forward to working with the OIG to identify the weaknesses that have the largest impact on the disclaimer condition, and will again focus our remediation efforts to achieve the greatest results.

We look forward to continuing to build our relationship with the OIG as we work to address these and any future changes facing HUD and the communities we serve. Specifically, we are focused on four areas of operational improvement: accountability, increased transparency, interagency collaboration, and a greater commitment to measuring outcomes.

These efforts will go a long way in making HUD more efficient and effective, and help to ensure the progress made this year continues to reap increasingly beneficial results. The entire HUD team is committed to tackling these challenges head-on. Working collaboratively with OIG, HUD will continue to identify and implement solutions that will help ensure weaknesses impacting the audit opinion are adequately addressed.

We appreciate that the OIG is committed to HUD's missions, and is working to help provide us with actionable recommendations that will improve operations.

OIG Evaluation of Agency Comments

Comment 1 HUD's CFO provided comments to our draft report on November 9, 2018. We reviewed management's response and determined HUD is generally in agreement with the internal control weaknesses cited in our report. We will work with HUD during the audit resolution process to evaluate HUD's progress in developing and implementing corrective action plans to address these findings.