Department of Housing and Community Development:

Housing Bond Funds Generally Have Been Awarded Promptly and in Compliance With Law, but Monitoring Continues to Need Improvement

November 2009 Report 2009-037

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November 10, 2009 2009-037

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As required by the Health and Safety Code, Division 31, sections 53533 and 53545, the California State Auditor presents its second audit in a series concerning the Housing and Emergency Shelter Trust Fund acts of 2002 and 2006.

This report concludes that the Department of Housing and Community Development (HCD) and the California Finance Housing Agency generally awarded funds in a timely manner and complied with legal requirements for making awards. However, HCD did not always adhere to controls it established for its CalHome Program. For example, as we reported in September 2007, HCD continues to advance funds to recipients, primarily individuals and local entities that ultimately receive the funds awarded, at amounts greater than limits set in their standard agreements. In addition, HCD did not always ensure that recipients submitted quarterly status reports as required in its regulations for the CalHome Program.

We also reported in 2007 that HCD did not have processes in place for conducting site visits of recipients or otherwise verifying program compliance during the period following final disbursement of funds for its CalHome and Emergency Housing and Assistance programs. During our current review, we found that HCD has developed monitoring processes for these programs. However, because of state budget difficulties, HCD restricted the amount of travel for performing on-site visits beginning in July 2008; thus, it has not met the goals it established for conducting on-site visits for these two programs in addition to a third program. Finally, HCD has not yet completed its verification of data transferred to its new Consolidated Automated Program Enterprise System, which it uses to administer and manage the housing bond programs.

Respectfully submitted,

Elaine M. Howle

ELAINE M. HOWLE, CPA
State Auditor

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Summary

Results in Brief

In 2002 and 2006 California voters passed the Housing and Emergency Shelter Trust Fund acts to provide bonds (housing bonds) for use in financing affordable housing for low- to moderate-income Californians. The Department of Housing and Community Development (HCD) and the California Housing Finance Agency (Finance Agency) primarily award, disburse, and monitor the housing bond funds received by various programs.

As of December 2008 HCD and the Finance Agency had awarded nearly all of the November 2002 bond funds to recipients, primarily individuals and local entities that ultimately receive the funds awarded. Additionally, although HCD and the Finance Agency awarded housing bond funds authorized in November 2006 for eight of the 10 programs that are within the scope of this audit in a timely fashion, HCD has not yet issued any awards for the remaining two programs. Because of circumstances surrounding the State's fiscal situation, HCD also experienced delays in disbursing both the 2002 and 2006 bond funds to recipients. However, both HCD and the Finance Agency have established and generally adhered to policies intended to ensure that only eligible applicants receive awards.

For disbursement of the housing bond awards, both agencies generally have processes in place to ensure that recipients meet legal requirements. However, HCD did not always adhere to the controls established for its CalHome Program. For example, it has continued to advance funds to recipients at amounts greater than the limit set in their standard agreements, a practice that we previously reported in September 2007 during our initial audit of these bond programs. In response to that audit, HCD implemented procedures that establish criteria for issuing advances constituting more than 25 percent of the total award. However, HCD did not follow these procedures for two of the 10 recipients we tested that received advances exceeding the limit. Establishing limits on the amounts advanced to recipients helps ensure that projects are, in fact, progressing before all funds are disbursed, and it also allows the State to maximize interest earnings.

In addition, HCD did not always ensure that recipients submitted quarterly status reports for its CalHome Program, as required in its CalHome regulations. HCD uses these reports, in part, to assess the performance of program activities. Also, the Finance Agency did not always ensure that its sponsors, comprising local entities qualified to construct or manage housing developments, had a regulatory agreement in place. These agreements provide assurance

Audit Highlights . . .

Our review revealed the following for the Housing and Emergency Shelter Trust Fund acts of 2002 and 2006:

- *As of December 2008 the Department of Housing and Community Development (HCD) and the California Housing Finance Agency (Finance Agency) had awarded nearly all the November 2002 bond funds.*
- *Although both HCD and the Finance Agency awarded housing bond funds authorized in November 2006 for eight of 10 programs in a timely fashion, HCD has not yet issued any awards for the remaining two programs.*
- *Both HCD and the Finance Agency have established and generally adhered to policies intended to ensure that only eligible applicants receive awards.*
- *For disbursement of the housing bond awards, both agencies generally have processes in place to ensure that recipients meet legal requirements; however, as we reported in September 2007, HCD continues to advance funds to recipients at amounts greater than the established limit for its CalHome Program.*
- *Because of state budget difficulties, HCD restricted travel, beginning in July 2008, for performing on-site monitoring visits. Thus, it has not met the goals it established for conducting such visits for its Emergency Housing, CalHome, and Supportive Housing programs.*

continued on next page . . .

» HCD has not yet completed its verification of data transferred to its new Consolidated Automated Program Enterprise System, which it uses to administer and manage the housing bond programs.

that developments being built using funds from the Residential Development Loan Program remain affordable to low- and moderate-income households.

We reported in 2007 that HCD did not have processes in place for conducting site visits of sponsors or otherwise verifying program compliance during the period following final disbursement of funds by the State for its CalHome Program and Emergency Housing and Assistance Program (Emergency Housing Program). During our current review, we found that HCD has developed monitoring processes for these programs, which were adopted in December 2007 and February 2008, respectively. However, because of state budget difficulties, HCD restricted the amount of travel for performing on-site visits beginning in July 2008; thus, it has not met the goals it established for conducting on-site visits for these two programs in addition to a third program we identified during our current review—its Multifamily Housing Program–Supportive Housing Program (Supportive Housing Program). In fact, HCD did not perform any on-site monitoring reviews for its Supportive Housing and CalHome programs during fiscal year 2008–09. However, HCD did perform on-site monitoring for its Emergency Housing Program, focusing on those sponsors it considered a higher risk. We believe focusing review efforts on the higher-risk sponsors for the Emergency Housing Program is a reasonable approach that HCD should consider adopting for the other two programs. By not monitoring at least the higher risk sponsors, HCD cannot ensure that sponsors use funds in accordance with housing bond requirements or that the programs are benefiting the intended populations. Moreover, for the on-site visits HCD performed for its CalHome Program prior to fiscal year 2008–09, it did not always communicate its findings and concerns to the sponsors in a timely manner. As a result, HCD cannot ensure that sponsors take timely and appropriate corrective action.

Further, we found that HCD continues to lack sufficient internal controls over its information technology system. Specifically, we noted during our September 2007 audit that HCD did not ensure the accuracy and completeness of the data converted into its Consolidated Automated Program Enterprise System (CAPES), which it uses to administer and manage various housing programs. In August 2008 HCD indicated that it expected all converted data would be validated and, where necessary, corrected by April 2009. However, as of September 2009, HCD still had not completed the data validation process, and it indicated that it does not expect to do so until March 2010.

Finally, the Housing and Emergency Shelter Trust Fund Act of 2006 (Proposition 1C) currently does not require the Bureau of State Audits (bureau) to conduct periodic audits of the

Transit-Oriented Development Implementation Program; the Regional Planning, Housing, and Infill Incentive Account; and the Housing Urban-Suburban-and-Rural Parks Account, which constitute $1.35 billion, or 47 percent of the Proposition 1C funds. For the bureau to perform periodic audits of these three programs, a change in the statute is necessary.

Recommendations

HCD should continue its efforts to monitor recipients of housing bond funds by doing the following:

- Follow its procedures on restrictions of bond fund advances that exceed 25 percent of the total award under the CalHome Program.

- Ensure that it receives and reviews required status reports from recipients of funds under its CalHome Program.

- When practical, adopt a risk-based, on-site monitoring approach for its CalHome and Supportive Housing programs similar to the monitoring methodology used for the Emergency Housing Program.

- Promptly communicate concerns and findings identified during on-site visits conducted for its CalHome Program.

To ensure that sponsors are using properties for the intended purposes of the Residential Development Loan Program, the Finance Agency should obtain signed copies of recorded regulatory agreements before disbursing funds to them.

To ensure that data maintained in CAPES are accurate and complete, HCD should complete its review of the accuracy of the data transferred to CAPES. HCD should also ensure that its cleanup efforts are thoroughly documented and retained for future reference.

If the Legislature believes that the bureau should perform periodic reviews of the bond programs not currently included in the audit requirements under Proposition 1C, it should propose legislation to require the bureau to do so.

Agency Comments

HCD and the Finance Agency agreed with our recommendations and indicated that they are moving forward to implement them.

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Introduction

Background

For 20 years, California voters and the Legislature for the State have supported numerous efforts to aid low- to moderate-income and homeless populations in securing housing and shelter. In the late 1980s and early 1990s, voters approved the issuance of $600 million in general obligation bonds to fund state housing programs. After the last of those bond funds were spent, the Legislature typically appropriated less than $20 million annually from the State's General Fund for the programs. In fiscal year 2000–01, however, the Legislature appropriated more than $350 million from the General Fund for housing programs. Then, in 2002 and in 2006, the Legislature proposed and the voters approved nearly $5 billion in Housing and Emergency Shelter Trust Fund Act bonds (housing bonds) to continue these efforts.

Housing and Emergency Shelter Trust Fund Act of 2002

In November 2002 California voters approved the Housing and Emergency Shelter Trust Fund Act of 2002 (Proposition 46), which provides $2.1 billion for the development of affordable rental housing, emergency homeless shelters, and down payment assistance to first-time, low- and moderate-income home buyers. Proposition 46 currently funds 23 housing programs: 12 programs already in existence when the bonds were approved and 11 new programs, nine established in 2002 and two established in 2005. The new programs include funds for down payment assistance to low-income, first-time home buyers and for supportive housing aimed at reducing homelessness. Proposition 46 allocates specific amounts for each of the programs, which are administered by either the Department of Housing and Community Development (HCD) or the California Housing Finance Agency (Finance Agency).

Figure 1 on the following page shows Proposition 46 funding by its four core areas, which we categorize and describe in the text box. The Appendix provides details on each program within the core areas.

Housing Bond Core Areas

Multifamily housing programs: Provide funding for constructing or renovating rental housing projects. They also fund supportive housing for disabled or homeless persons. Funding generally takes the form of low-interest loans to recipients to partially fund the cost of construction.

Home ownership programs: Encourage home ownership by offering low-interest loans or grants that help low- to moderate-income Californians meet down-payment requirements.

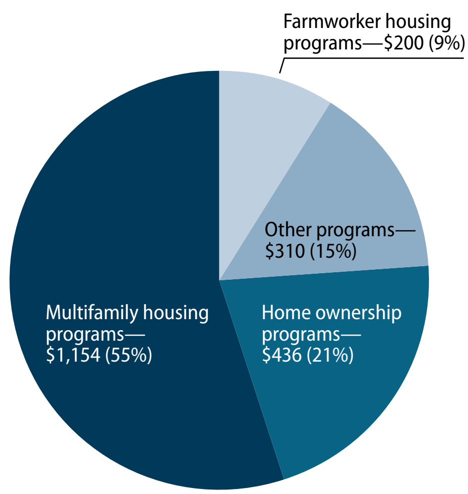
Farmworker housing programs: Provide funding for the construction or rehabilitation of housing for agricultural employees and their families. Funds support for both rental and owner-occupied housing.

Development programs: Promote projects such as parks, water, sewage, transportation, and housing in existing urban areas and near public transportation. (This core program area applies only to funds available through the Housing and Emergency Shelter Trust Fund Act of 2006.)

Other programs: Provide funding for developing emergency homeless shelters and transitional housing, incentives to cities and counties based on the number of new housing units approved, mortgage insurance for high-risk home buyers, and capital needs of local government agencies responsible for enforcing housing codes.

Sources: Legislative Analyst's Office analyses of the 2003–04 Budget Bill and Implementation of the Housing Bond, dated March 28, 2007.

Figure 1
Proposition 46 Allocations by Core Area
(Dollars in Millions)



Sources: California Health and Safety Code, Division 31, Part 11, and the Department of Housing and Community Development's *Cumulative Proposition 46 Bond Awards Report Through December 31, 2008*.

Note: For some programs, Proposition 46, the Housing and Emergency Shelter Trust Fund Act of 2002, requires that funds not awarded within a certain time frame revert to other housing bond programs. The amounts shown represent funding available as of December 31, 2008, and may not agree with the original funding level for programs presented in the law.

Many of the laws governing Proposition 46 programs also restrict administrative costs. These restrictions generally limit the amount of funding HCD and the Finance Agency can use for administrative support to between 3 percent and 5 percent of individual program allocations.

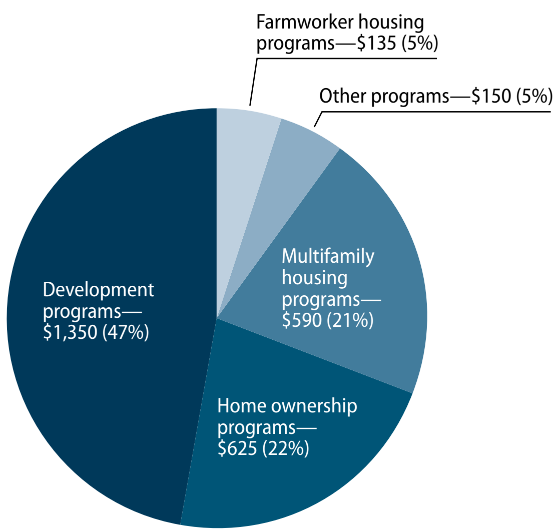
Housing and Emergency Shelter Trust Fund Act of 2006

In November 2006 California voters approved the Housing and Emergency Shelter Trust Fund Act of 2006 (Proposition 1C). It provides nearly $2.85 billion to support the same four core areas as Proposition 46, plus a fifth one—development programs—that focuses on infrastructure. (See the text box on the previous page.)

Proposition 1C funds 13 housing programs, nine of which existed before the passage of the proposition. Three of the four new programs established in 2006 support urban development and parks, while the fourth is aimed at encouraging cost-saving approaches to create or preserve affordable housing. Three of the four new programs established by Proposition 1C and included under the development program's core area—the Transit-Oriented

Development Implementation Program; the Regional Planning, Housing, and Infill Incentive Account; and the Housing Urban-Suburban-and-Rural Parks Account—constitute $1.35 billion (47 percent) of the total funds authorized. As we describe later in the Scope and Methodology section of this report, the Bureau of State Audits (bureau) is not required to audit these three programs. Thus, our audit focuses only on the remaining Proposition 1C programs, which constitute $1.5 billion of the bond funds. Figure 2 shows Proposition 1C funding by core area.

Figure 2
Proposition 1C Funding by Core Area
(Dollars in Millions)



Source: California Health and Safety Code, Division 31, Part 12.

Suspension of Most Bond Activities

As a result of the State's budget crisis, in December 2008 the Department of Finance (Finance) directed all state agencies that have expenditure control and oversight of general obligation bond programs to cease authorizing any new grants or obligations for bond projects. It also froze bond-related disbursements to recipients except for necessary administrative costs. In March, April, and October 2009 the State issued new general obligation bonds. From these bond proceeds, HCD indicated it received more than $850 million intended for the purpose of meeting the cash disbursement demands of recipients that received awards before December 2008. Although HCD may now disburse funds to these recipients, it is still prohibited from authorizing new bond awards. As of October 2009 Finance has not indicated when state agencies may resume normal operation of general obligation bond programs.

Department of Housing and Community Development

HCD is the State's lead housing agency. Its mission is to provide leadership, policies, and programs to preserve and expand safe and affordable housing opportunities and promote strong communities for all Californians. With more than 620 employees and a budget of about $1 billion for fiscal year 2008–09, HCD focuses its efforts through three major divisions—Financial Assistance, Housing Policy Development, and Codes and Standards. The divisions of Financial Assistance and Housing Policy Development award the grant and loan funds available from the housing bonds. The Financial Assistance Division also offers technical assistance, promotes economic development, and manages HCD's portfolio of loans and grants.

HCD directly administers 21 of the 28 housing bond programs, and the Finance Agency is responsible for the day-to-day management of the other seven programs. Additionally, through separate legislation, the Legislature appropriated a portion of the funds from the Regional Planning, Housing, and Infill Incentive Account to a new program—the California Recycle Underutilized Sites Program—which is administered by the California Pollution Control Financing Authority under the State Treasurer's Office.

Housing Bond Recipients

Sponsors: Local public entities; nonprofit corporations; joint ventures; partnerships; limited partnerships; trusts; corporations; cooperatives; and individuals qualified to own, construct, or rehabilitate housing developments.

Home buyers: Persons, generally purchasing homes for the first time and of low- to moderate-income, who receive assistance through housing bond programs.

Sources: Department of Housing and Community Development's Web site and the California Health and Safety Code, Division 31, various sections.

Most programs operated directly by HCD provide funding to sponsors (see the text box) that construct or manage housing projects. In many cases, these sponsors in turn provide services to the beneficiaries targeted by the programs. Typically, housing bond funds only partially finance projects. As of December 31, 2008, in addition to the $2.9 billion it awarded, HCD reported that its recipients received nearly $21 billion from other funding sources.

California Housing Finance Agency

As the State's affordable housing bank, the Finance Agency supports the needs of renters and first-time home buyers by offering financing and programs that create opportunities for safe, decent, and affordable housing for individuals within specified income ranges. Under interagency agreements with HCD, the Finance Agency directly manages seven Proposition 46 programs.

In August 2007 the two parties executed another agreement for the Finance Agency to manage one program under Proposition 1C. In addition to supporting the programs funded by the propositions, the Finance Agency provides loans to home buyers and sponsors of affordable rental housing through the sale of tax-exempt and taxable bonds unrelated to the housing bonds.

With more than 300 employees and a budget of about $45.9 million in fiscal year 2008–09, the Finance Agency addresses its mission through four types of programs: mortgage insurance, home ownership, multifamily, and special lending programs. Mortgage insurance programs aid first-time home buyers, low- to moderate-income borrowers, and individuals who may not qualify for traditional lending programs by providing primary mortgage insurance at favorable rates.

Home ownership programs aim to provide affordable housing opportunities by offering mortgages to first-time home buyers with low to moderate incomes. According to its Web site, the Finance Agency has helped more than 150,000 Californians purchase their first homes by issuing a total of $18 billion in loans since 1976. Its Web site also reports that the Finance Agency's portfolio contains almost 32,000 home mortgage loans valued at a total of $6.1 billion. The Finance Agency does not lend money directly to borrowers. Rather, private lenders that it has approved verify applicants' qualifications and offer mortgage loans. After the Finance Agency reviews the closing documentation and ensures that certain requirements are met, it purchases the mortgage loans from the lenders and assumes responsibility for servicing some of the loans.

Multifamily programs provide permanent financing for the acquisition, rehabilitation, and preservation of existing rental housing, as well as the construction of new rental housing. The role of these programs is to finance rental housing for very low- to moderate-income individuals and families, and for special needs households. According to its Web site, since its inception in 1975, the Finance Agency has made nearly $1.7 billion in loans for multifamily housing projects, financing 415 projects that provide more than 33,300 housing units. Finally, the role of the special lending programs is to administer unique lending activities that benefit low- and moderate-income families. The objective is to develop innovative financing for affordable housing with housing sponsors in markets that are not addressed through the Finance Agency's conventional financing.

Scope and Methodology

The California Health and Safety Code requires the bureau to conduct periodic audits of housing bond activities to ensure that proceeds are awarded in a manner that is timely and consistent with legal requirements and that recipients use the funds in compliance with the law. Although Section 53533(d) requires the bureau to perform periodic audits on all programs funded by Proposition 46, Section 53545(a)(3) does not require it to conduct periodic audits of three programs included in Proposition 1C: the Transit-Oriented Development Implementation Program; the Regional Planning, Housing, and Infill Incentive Account; and the Housing Urban-Suburban-and-Rural Parks Account. Thus, we did not audit these three programs.

To determine whether awards of housing bond funds were timely, we reviewed the propositions, prior audits, and other laws to clarify the definition of *timely*. Because the law does not define *timely*, we concluded that HCD's estimated awards established in 2002 and revised in 2007, and the Finance Agency's estimated awards established in 2003, are the most appropriate criteria against which to assess the timeliness of the actual awards. For Proposition 46 awards, we examined both entities' initial award schedules. HCD anticipated awarding nearly all Proposition 46 funds available for recipients by June 30, 2008, while the Finance Agency anticipated awarding 94 percent by that same date. Therefore, in the absence of a specific definition of timeliness in statute, we judgmentally determined that, to be considered timely, they should have awarded at least 90 percent of their bond funds by December 31, 2008—the date of HCD's most recent award-tracking system report available at the time of our fieldwork. For those programs for which HCD and the Finance Agency had not yet awarded 90 percent of the bond funds, we interviewed program staff to obtain an understanding of the reasons and assessed whether these explanations seemed reasonable.

For Proposition 1C programs, we reviewed those programs for which HCD or the Finance Agency had yet to award any funds or had awarded only a small percentage and compared them to the award schedule. We again asked program staff to provide explanations and supporting documentation for why funds were not being awarded more quickly and assessed the reasonableness of their explanations.

To assess whether HCD and the Finance Agency awarded funds in compliance with applicable statutory requirements, we selected three programs with significant propositions 46 and 1C awards and disbursements through December 31, 2008, that we had not reviewed in our previous audit. These programs were the Multifamily Housing Program–Supportive Housing Program; the Workforce Housing Reward Program; and the Residential Development Loan Program, which the Finance Agency administers. We also selected for review two other programs—HCD's CalHome Program and the capital development portion of the Emergency Housing and Assistance Program—because we had reported issues related to these two programs in our previous report.

As of December 31, 2008, the five programs we selected accounted for 30 percent of the Proposition 46 funds awarded. Of these five programs, four were authorized to receive funding under Proposition 1C; however, the Finance Agency discontinued one of the programs because of a lack of interest on the part of those the program was designed to serve, and HCD had not awarded any funds for another program as of December 31, 2008. The remaining two programs accounted for 34 percent of the Proposition 1C funds awarded, excluding those programs not subject to our audit.

To ensure that the total of all awards granted by each program did not exceed the funding limit established in law, we analyzed information from the award-tracking system. Further, based on our review of relevant laws and regulations, we identified key legal provisions that the programs must implement when awarding funds. We judgmentally selected 43 awards granted by the four HCD-administered programs and five of the 12 awards from the Finance Agency's Residential Development Loan Program. In selecting our sample of awards, we considered factors such as geographic distribution, type of sponsor, and amount of award—the largest of which was nearly $9.7 million. We then tested those awards to assess whether the entities met key legal provisions.

To determine whether recipients complied with applicable statutes, we reviewed relevant laws, regulations, program guidelines, policies, and procedures and interviewed officials to determine how HCD and the Finance Agency monitor recipients throughout the term of the award. We judgmentally selected 36 awards from the four HCD-administered programs and five awards from the Finance Agency's Residential Development Loan Program to assess whether the entities implemented processes that would allow them to ensure that recipients used housing bond funds in compliance with the law. Further, we tested whether HCD and the Finance Agency followed those processes.

The U.S. Government Accountability Office, whose standards we follow, requires us to assess the reliability of computer-processed data. To determine the amount of awards and disbursements by program, we used data from five systems used by HCD and the Finance Agency. Table 1 on the following page shows the results of our review. We assessed the reliability of the data of the systems shown in the table by performing electronic testing of key data elements and by testing the accuracy and completeness of the data. To test the accuracy of the data, we selected a random sample of awards from four of the five systems and reconciled key data elements to the source documents included in the files located at HCD and the Finance Agency. Generally, we performed completeness testing by selecting a sample of contract files and comparing information from documents contained in the files to key data elements. However, for the Finance Agency's Lender Access System, we performed completeness testing by examining the gaps in loan numbers. Further, because the Finance Agency had awarded relatively few contracts for its Residential Loan Development Program, we tested the entire population for accuracy and completeness.

Table 1
Reliability of the Databases Used by the Department of Housing and Community Development and the California Housing Finance Agency That We Tested

ENTITY	SYSTEM	PURPOSE FOR WHICH THE DATA WERE USED	RELIABILITY DETERMINATION FOR THE PURPOSES OF THIS AUDIT
Department of Housing and Community Development (HCD)	Cumulative propositions 46 and 1C bond awards spreadsheet	Amount of awards	Sufficiently reliable
	California State Accounting and Reporting System	Amount of disbursements	Sufficiently reliable
California Housing Finance Agency (Finance Agency)	Residential Development Loan Program spreadsheet	Amount of awards and disbursements	Sufficiently reliable
	Lender Access System	Amount of awards and disbursements	Sufficiently reliable
	School Facility Fee System	Amount of awards and disbursements	Undetermined*

Sources: Bureau of State Audits' analyses of databases obtained from HCD and the Finance Agency.

* We were unable to verify the completeness of this system.

As also shown in Table 1, we determined that the Finance Agency's School Facility Fee System data were of undetermined reliability for the purpose of determining the amount of awards and disbursements. We identified multiple entries for the same award in the file that indicated whether a loan had been made. According to Finance Agency staff, these entries were most likely caused by either a conversion error or a program processing error. Although it is unlikely that these errors affected our analysis, we cannot be certain that records were not incorrectly created to indicate that a loan had been made when it had not. Additionally, we were unable to fully test the School Facility Fee System data for completeness, because we were unable to select a sample of awards to trace into the system and could not identify another method that we could use to test completeness. We found that the remaining four systems were sufficiently reliable for purposes of this audit.

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Audit Results

Awards of Housing Bond Funds Were Generally Timely

In most cases, the Department of Housing and Community Development (HCD) and the California Housing Finance Agency (Finance Agency) have awarded funds from the bonds (housing bonds) issued under the Housing and Emergency Shelter Trust Fund acts of 2002 and 2006 (Proposition 46 and Proposition 1C, respectively) in a timely manner. Although HCD and the Finance Agency anticipated awarding nearly all of the Proposition 46 funds available for recipients, excluding administrative costs, by the end of fiscal year 2007–08, three of the 23 programs still had more than 10 percent of these funds remaining to award. Furthermore, HCD has yet to make any awards for two of 10 programs funded by Proposition 1C, citing several reasons for not doing so.

HCD and the Finance Agency Have Awarded Nearly All of Their Proposition 46 Funds

As the direct administrators for many of the State's housing bond programs, HCD and the Finance Agency had awarded, by December 31, 2008, almost all housing bond funds available for recipients under Proposition 46. Although Proposition 46 authorizes $2.1 billion for housing bond programs, a portion is reserved for the State's administrative costs, leaving $1.9 billion for awards to recipients. In December 2008 HCD reported that it had awarded 95 percent of the $1.6 billion available for loans and grants to recipients. Additionally, the Finance Agency's records showed that it had awarded 95 percent of the $284 million available for awards to recipients.

HCD reported the total amount awarded by each program in its report titled *Cumulative Proposition 46 Bond Awards Report Through December 31, 2008*, which is available to the public on its Web site.[1] It excludes from its calculation funds that recipients have returned, a practice that seems reasonable because HCD cannot control when a recipient chooses not to move forward on a project or spends less than anticipated. Using its December 31, 2008 report, we calculated that for 14 of the 16 Proposition 46 programs it is responsible for, HCD had awarded at least 90 percent of the bond funds available for recipients.

[1] The December 31, 2008, report was the most recent report available at the time of our fieldwork, and HCD indicated that it was still finalizing the next report as of September 2009. Also, as we discuss in the Introduction, HCD did not award funds between January and June 2009; therefore, this report generally reflects the most current amounts awarded at the time of our fieldwork.

In April 2002 HCD prepared an estimated annual award schedule (award schedule) outlining, by fiscal year and program, the amounts it anticipated awarding if Proposition 46 were to pass in November 2002. In December 2007 it revised its award schedule to reflect its most current plans. Before voters approved the Proposition 46 bonds, HCD undertook efforts to determine the needs of the prospective bond-related programs. That effort helped it to develop regulations and guidelines, establish detailed timelines, and determine staffing needs. HCD stated that it determined the level of funding recipients could handle on an annual basis by meeting with stakeholders and relying on its experience administering other housing programs. HCD indicated that based on this information, it spread the awards over several years to ensure increased competition for the funds and higher quality projects. Its eight-year award schedule shows total authorized funding, support costs, and estimated awards by fiscal year. In determining the total amount available to award, HCD set aside a portion of the bond funds for costs related to administering the bond programs and reserves. In each award schedule, it projected that it would have awarded nearly all its Proposition 46 funds available for recipients by the end of fiscal year 2007–08.

As of December 31, 2008, HCD reported that it had awarded less than 90 percent of the bond funds available for recipients of two of the 16 Proposition 46 programs for which it is responsible.

However, as of December 31, 2008, HCD reported that it had awarded less than 90 percent of the bond funds available for recipients of two of the 16 Proposition 46 programs for which it is responsible. Specifically, for the Downtown Rebound Program, HCD had awarded 87 percent, and for the Governor's Homeless Initiative it had awarded 63 percent. The funding for the Downtown Rebound Program was not authorized by statute until November 2004, and the Governor's Homeless Initiative was not established by the governor until August 2005. Because these two programs did not begin as early as other programs supported by Proposition 46 funds, it seems reasonable that HCD would have awarded a lower percentage of funds for these two programs, compared to the percentages for the other 14 programs.

The Finance Agency also has a process for estimating annual awards. In 2003 it developed a five-year business plan (covering fiscal years 2003–04 through 2007–08) that included anticipated awards under its six Proposition 46 programs. The 2003 business plan did not include a seventh program, the Residential Development Loan Program, which was not legally established and funded until 2005. The 2005 statute redirected a portion of the funds from one of the other six programs—the California Homebuyer's Downpayment Assistance Program—to this seventh program. The Finance Agency estimated that it would award $291.3 million, or 94 percent, of its Proposition 46 funds available for recipients by the end of fiscal year 2007–08. In fact, the Finance Agency had awarded 95 percent by December 2008.

The Finance Agency had awarded 95 percent of its Proposition 46 funds by December 2008, which seems reasonable when compared to the 94 percent it estimated it would award six months earlier.

On the other hand, as of December 31, 2008, the Finance Agency had awarded only 63 percent, or just over $29 million, of the bond funds available for recipients of its Homebuyer's Downpayment Assistance Program–School Facility Fee. This program reimburses qualified buyers of newly constructed homes for a portion or all of the school facilities fees paid by the builder. The buyer can use this amount to pay the costs associated with a first mortgage loan, such as a down payment or closing costs. The Finance Agency estimated that it would award, in total, $34 million for this program by the end of 2008. As of December 31, 2008, however, it had awarded only $29 million, or about 15 percent less than it had projected. According to the Finance Agency, it has been awarding funds for this program to all eligible buyers that applied for an award. Thus, although we cannot definitively conclude whether the amount the Finance Agency had awarded as of December 31, 2008, is timely because the statutes do not provide a specific definition for timely, the Finance Agency has provided a reasonable explanation—a lesser demand for these program funds than it originally estimated—for making fewer awards for this program.

Proposition 1C Bond Funds Were Usually Awarded in a Timely Manner, Although HCD Has Yet to Award Any Funds for Two Programs

HCD and the Finance Agency promptly awarded a reasonable proportion of the funds available to recipients for eight of the 10 programs funded by Proposition 1C.[2] However, HCD has yet to award any funds for the two remaining programs. From the initial authorization of Proposition 1C bonds in November 2006 until December 2008, HCD and the Finance Agency awarded between 24 percent and 68 percent of the bond funds available to recipients for eight of the programs. Overall, they awarded 44 percent, or $602 million, of the $1.2 billion in total bond funds available under Proposition 1C within this two-year period, as shown in Table 2 on the following page. HCD's award schedule estimates that 92 percent, or almost $1.4 billion, of the bond funds for the programs subject to our audit will be awarded by the end of fiscal year 2010–11. If HCD continues to award housing bond funds at the same rate over the current and next fiscal year, it should meet or exceed its estimate.

[2] When determining whether housing bond funds were awarded in a timely fashion, we did not assess those programs that are outside the scope of this audit: the Transit-Oriented Development Implementation Program; the Regional Planning, Housing, and Infill Incentive Account; and the Housing-Urban-Suburban-and-Rural Parks Account.

Table 2
Proposition 1C Percentages of Available Bond Funds Awarded by Program as of December 31, 2008

CORE PROGRAM AREA AND PROGRAM NAME	PERCENTAGE OF AVAILABLE PROGRAM FUNDS AWARDED
Multifamily Housing Programs	
Multifamily Housing Program—General	68%
Multifamily Housing Program—Supportive Housing Program	46
Multifamily Housing Program—Homeless Youth	47
Home Ownership Programs	
CalHome Program	52
Building Equity and Growth in Neighborhoods	34
California Self-Help Housing Program	25
California Homebuyer's Downpayment Assistance Program*	24
Farmworker Housing Programs	
Joe Serna, Jr. Farmworker Housing Grant Program—General	49
Other Programs	
Affordable Housing Innovation Fund	0
Emergency Housing and Assistance Program	0
Percentage Awarded of the Total Proposition 1C Funds Available	**44%**

Sources: *Cumulative Proposition 1C Bond Awards Report as of December 31, 2008*, and California Housing Finance Agency (Finance Agency) purchased loans report as of December 2008.

Note: Proposition 1C is the Housing and Emergency Shelter Trust Fund Act of 2006. Programs not subject to this audit do not appear in this table.

* The Finance Agency administers this program.

However, as of December 2008, HCD had not awarded any Proposition 1C funds for two of its programs: the Emergency Housing and Assistance Program (Emergency Housing Program) and programs authorized under the Affordable Housing Innovation Fund. HCD explained that Proposition 46 also authorized funding for the Emergency Housing Program, and it stated that it intends to award all Proposition 46 funds available for this program before it awards any funds from Proposition 1C. HCD indicated that Proposition 46 provided sufficient funds to cover awards to all qualified applicants through December 2008 and stated that it does not anticipate using Proposition 1C funds for this program until the 2009 funding round. We believe HCD's decision to use Proposition 46 funds first is reasonable and adequately explains the delay in awarding Proposition 1C funds to this program. Moreover, in July 2009 HCD announced the conditional awarding of $7 million in Proposition 1C funds for the Emergency Housing Program. We discuss the nature of these conditional awards in a later section of this report.

HCD delayed implementation of the programs authorized under the Affordable Housing Innovation Fund for three reasons. First, Proposition 1C established this fund and allocated $100 million to it. However, the proposition indicated that the specific criteria establishing program eligibility and the allowable use of the funds would be established through separate legislation. In October 2007 the Legislature enacted legislation creating several programs under the Affordable Housing Innovation Fund and establishing their eligibility criteria—almost a year after the voters authorized the use of Proposition 1C funds—and this time interval, according to HCD, contributed to the delay in awarding funds under these programs.

In addition, HCD elected to postpone implementing these programs because it decided to focus first on implementing two new, larger programs established by Proposition 1C—the $850 million Regional Planning, Housing, and Infill Incentive Account and the $300 million Transit-Oriented Development Implementation Account. HCD believes that the programs funded under these two accounts will have a greater impact on the State's overall affordable housing situation because they address both rental housing and home ownership, while the programs funded under the Affordable Housing Innovation Fund address only home ownership. HCD added that it is directing its limited resources to the projects that will lead to the greatest economic benefits, such as increasing the number of jobs.

HCD also elected to postpone implementing the programs under the Affordable Housing Innovation Fund, deciding to focus first on implementing the two new, larger programs established by Proposition 1C.

Finally, HCD stated that complications arising from implementing the programs under the Regional Planning, Housing, and Infill Incentive Account and the downturn in the financial markets further contributed to the delay in implementing the programs under the Affordable Housing Innovation Fund. HCD originally anticipated making funds available from this fund in late 2008 and early 2009. However, the delay in the enactment of the fiscal year 2008–09 budget and the Department of Finance's (Finance) suspension of funding activity in December 2008 resulted in HCD soliciting applications for only one program under the Affordable Housing Innovation Fund and postponing its solicitation of applications for several others. As of July 2009 HCD still had not awarded funds under any of the programs. However, HCD's explanations for its delay in awarding these funds have merit.

HCD and the Finance Agency Usually Complied With Legal Requirements When Awarding Housing Bond Funds

HCD and the Finance Agency distributed bond funds in accordance with statutory limits. For example, in determining the funds available for grants and loans, HCD proportionally distributed statewide costs among the programs and appropriately earmarked funds for program administration. Both entities awarded housing bond funds for the intended programs to the correct types of sponsors and for the proper activities. For instance, they generally provided the necessary documentation showing that their applicants met eligibility requirements, and they used established selection criteria when awarding funds. For the CalHome Program, HCD verified that sponsors—recipients that provide services to targeted beneficiaries of the program—were either local governments or nonprofit organizations and ensured that proposed activities involved low-income individuals who were first-time home buyers needing mortgage assistance or owner-occupants in need of housing rehabilitation. Likewise, for the Multifamily Housing Program–Supportive Housing Program (Supportive Housing Program), HCD checked that sponsors had demonstrated prior experience in the ownership or operation of a rental housing development and that those projects included construction or rehabilitation of rental housing.

Types of Set-Aside Costs

Statewide costs: Expenses, including bond issuance costs, incurred by the State Treasurer's Office, the State Controller's Office, and the Department of Finance.

Administrative support costs: Costs associated with the administration and coordination of the housing bond programs.

Default reserves: Amounts for unexpected costs incurred to protect the State's security interest. The Department of Housing and Community Development could eventually disburse unused reserves in the form of loans and grants.

Sources: California Health and Safety Code, Division 31; California Government Code, Section 16724.6; State Administrative Manual, Section 9220.3; and Department of Housing and Community Development staff.

HCD ensured that it did not exceed limits on administrative costs set in the law for all programs involving housing bond funds by periodically reviewing these costs and the amounts already awarded as loans and grants. It prepared an analysis estimating the distribution of administrative costs, referred to as set-aside costs, for Proposition 46 funds and developed a similar analysis for Proposition 1C funds. Both analyses identified amounts set aside in three areas: statewide costs, administrative support costs, and default reserves. (See the text box.)

According to HCD's most recent analyses, developed in June 2008, it anticipates using a total of $177 million, or 8.4 percent, of Proposition 46 bond funds for all three types of set-asides. It also expects to use $125.4 million, or 8.4 percent, of Proposition 1C bond funds for all the set-asides related to the programs that are subject to our audit. The set-aside costs for administrative support and statewide costs reduce the total amount of funding available for grants and loans. However, default reserves not used to support existing projects could eventually be awarded to new projects. Additionally, the State's General Obligation Bond Law allows a portion of any fund created to account for bond proceeds to be used to pay statewide costs. Thus, as part of the 8.4 percent, HCD set aside 2 percent of each program's funding for this purpose.

Most of the housing bond programs have set-asides of 5 percent or less for administrative support costs. For programs in which statute establishes a limit on the amount of bond proceeds that can be set aside for administrative support costs, we ensured that these costs did not exceed statutory limits. However, the administrative support costs that HCD set aside for the Joe Serna, Jr. Farmworker Housing Grant Program were 11.3 percent of the program's Proposition 46 funds and 9.1 percent of its Proposition 1C funds. Unlike some others, this program has no statutory limitation on administrative support costs. One reason for this higher percentage could be that, according to HCD, this program has long-term monitoring requirements that can last up to 55 years. These requirements include assessing the fiscal integrity of the project as well as verifying tenant eligibility. HCD stated that its administrative support cost set-asides include the cost of monitoring this program for up to 55 years.

HCD and the Finance Agency award housing bond funds through an application review and approval process that is program specific. At the end of this process, each agency makes a commitment to fund certain grants or loans. Generally, for the five programs we reviewed, HCD and the Finance Agency established and adhered to processes for identifying eligible sponsors and for properly making awards. For example, for the CalHome and Emergency Housing programs, HCD's eligibility determination included verifying nonprofit status and establishing whether the applicant had prior experience with or the capacity to perform program activities. Similarly, the Finance Agency's program staff assured that each applicant for the Residential Development Loan Program was a city, county, housing authority, or redevelopment agency.

For the five programs we reviewed, HCD and the Finance Agency generally established and adhered to processes for identifying eligible sponsors and for properly making awards.

HCD has processes to rank the applicants for programs required to use a competitive process. For instance, the CalHome Program issues notices of funding availability (notices) to solicit applications. Following the competitive process detailed in the notices, HCD evaluates, for example, the applicants' ability to provide loan services to low-income households for mortgage assistance or to owner-occupants for rehabilitation of their primary residence. Using this evaluation, HCD ranks the applicants. We found that for this program HCD ranked applicants according to scores from highest to lowest, eliminated any that did not meet minimum requirements, and awarded funds in rank order until the money was exhausted. In some cases, applicants that received relatively low scores under the competitive ranking process did not receive an award.

Although certain programs require a competitive process, at times the amount of funds HCD has available in an application period exceeds the amounts that eligible applicants request.

Although certain programs require a competitive process, at times the amount of funds HCD has available to award in an application period exceeds the total amounts requested by eligible applicants. As a result, it awards funds to all eligible applicants. For example, although HCD scored and ranked applicants based on their ability to meet program requirements for the Emergency Housing Program, the program manager indicated that HCD awarded funds to all eligible applicants for this program in 2006 and 2007. Similarly, the Finance Agency intended to rank competitively the applicants for its Residential Development Loan Program, but stated that it awarded funds to all eligible applicants because demand for funding has not exceeded the funding offered since the inception of the program.

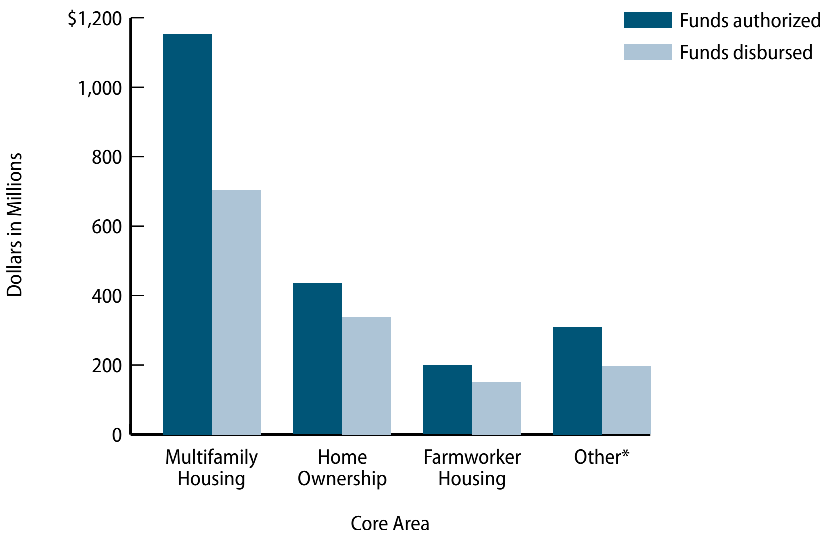
In our September 2007 audit of the housing bond funds, we reported that poor file management in its Emergency Housing Program made it impossible for us to verify whether HCD always used established selection criteria when awarding funds for this program in fiscal years 2002–03 through 2004–05. During our current review, we found that HCD had improved its file management because we were able to locate documents it used to assess applicant eligibility within the program files without difficulty. According to HCD, it created a new filing system and now uses a checklist to ensure that current files contain all necessary items in the proper order. In addition, HCD stated that as of May 2009 it is in the process of reorganizing older files using the new filing system.

The Disbursement of Bond Funds Has Been Much Slower Than the Awarding of Funds

By May 2009 HCD had disbursed about 67 percent of the total bond funds it administers related to Proposition 46 and 19 percent of the amounts awarded for programs within the scope of this audit under Proposition 1C. Given the long-term nature of some of its projects, this low percentage is to be expected. In December 2008, as a result of the State's budget crisis, Finance directed state agencies to cease authorization of new obligations or grants for bond programs. HCD responded by issuing conditional awards to applicants with the understanding that the disbursement of funds would be delayed.

As of May 2009 HCD had disbursed $1.4 billion of the $2.1 billion authorized under Proposition 46. In addition to disbursing bond funds to recipients based on program requirements and the terms of their awards, HCD transfers bond funds to the Finance Agency upon request for programs the Finance Agency manages. As discussed in the Introduction, Proposition 46 funding is categorized into four core areas. Figure 3 shows that the core area of multifamily housing programs has had the highest amount of disbursements but the lowest ratio of funds disbursed to funds authorized. This situation is not surprising, because for programs within this core area, HCD anticipates a two- to four-year lag between a sponsor's application and its loan closing, which is when the sponsor receives funds from HCD.

Figure 3
Proposition 46 Funds Authorized Compared to Funds Disbursed, by Core Area



Sources: California Health and Safety Code, Division 31, Part 11; the Department of Housing and Community Development's *Cumulative Proposition 46 Bond Awards Report Through December 31, 2008*; the reconciliation of the State Controller's Office appropriation balances with unexpended balances as of May 31, 2009; and the California Housing Finance Agency's awards database.

Note: Proposition 46 is the Housing and Emergency Shelter Trust Fund Act of 2002. The above disbursement figures include administrative costs. For some programs, Proposition 46 requires that funds not awarded within a certain time frame revert to other housing bond programs. The amounts shown represent funding available as of December 31, 2008, and may not agree with the original funding level for programs presented in the law.

* The "Other" core area consists of the Code Enforcement Incentive Program, the Emergency Housing and Assistance Program, the Workforce Housing Reward Program, and the Mortgage Guaranty Insurance Program.

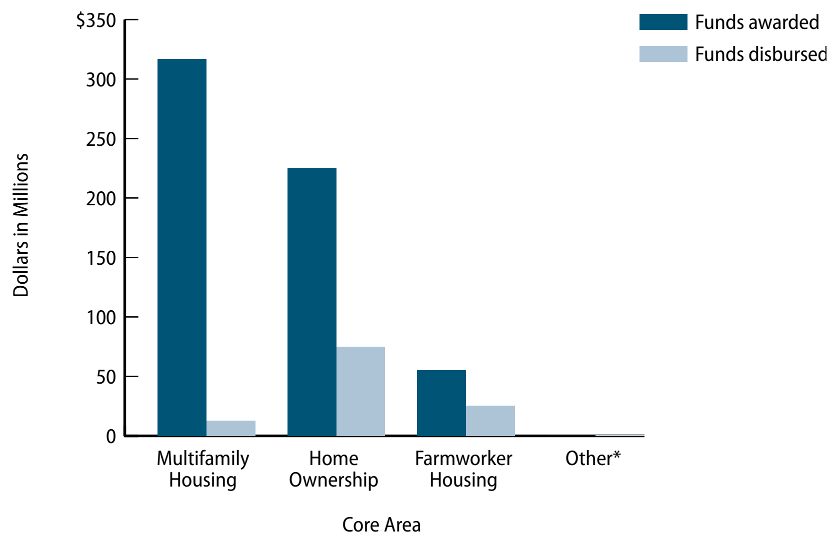
As of May 2009 HCD had disbursed $114 million of the more than $600 million in Proposition 1C funds it had awarded as of December 2008 for programs within the scope of this audit.[3]

[3] As discussed earlier in the report, we relied upon HCD's cumulative bond reports as of December 31, 2008, because they were the most current reporting of bond awards at the time of our fieldwork. The most current disbursement information at the time of our fieldwork was as of May 31, 2009.

Figure 4 shows a significant lag between award and disbursement. Multifamily housing programs had the smallest proportion of disbursements to awards, for the reasons indicated previously. Additionally, Figure 4 reflects that HCD had not yet awarded any funds in the *other programs* core area, which includes the Affordable Housing Innovation Fund and the Emergency Housing Program.

Figure 4

Proposition 1C Funds Awarded Compared to Funds Disbursed, by Core Area



Sources: The Department of Housing and Community Development's (HCD) *Cumulative Proposition 1C Bond Awards Report Through December 31, 2008*; the reconciliation of the State Controller's Office appropriation balances with unexpended balances as of May 31, 2009; and the California Housing Finance Agency's awards database.

Note: Proposition 1C is the Housing and Emergency Shelter Trust Fund Act of 2006. The above disbursement figures include administrative costs. HCD began expending Proposition 1C funds for administrative costs for the "Other" core area programs, but it has yet to make an award.

* The "Other" core area consists of the Affordable Housing Innovation Fund and the Emergency Housing and Assistance Program.

As discussed in the Introduction, according to HCD, it received more than $850 million in bond proceeds from the State's general obligation bond sales in March, April, and October 2009 intended to meet its cash disbursement needs for projects awarded before December 2008. According to HCD, it projects that this amount will be sufficient to cover its disbursement needs until about December 2009. However, Finance's direction to state agencies to cease authorization of new obligations or grants for bond projects may play a role in delaying the disbursement of some funds. HCD told us that it is continuing to award funds to applicants but warns them that disbursements may be delayed. HCD calls these *conditional awards*. It received approval from Finance to issue awards in this manner and indicated that it plans to continue awarding the remaining bond funds subject to Finance's approval until Finance reverses its suspension.

In addition, although it cannot commit to a time frame on the disbursement of awards made after December 2008, HCD stated that continuing the awards process is important because receiving a conditional award assists the recipient in obtaining the other financial resources it needs to complete the project. According to HCD, as of June 2009, Finance could not predict when the State will be in a condition financially to return to the bond market. Under these conditions, recipients have no assurance as to when they will actually receive the awarded funds. In July 2009 HCD announced it had awarded $714 million in conditional awards under programs funded by Proposition 1C.

Although HCD and the Finance Agency Have Monitoring Processes in Place, They Did Not Always Follow Them

Both HCD and the Finance Agency have established procedures for monitoring sponsors' use of funds and ensuring that occupants of bond-funded housing meet eligibility requirements. However, for three of the five programs we reviewed, they did not always follow them. As a result, they could not always ensure that sponsors for these three programs used funds in accordance with grant requirements or that the programs benefited only targeted populations. Regardless of the type of housing assistance provided by bond-supported programs, monitoring comprises two phases: disbursement and completion (see the text box).

Monitoring Phases for Housing Bond Programs

Disbursement phase: Period from award commitment to final state payment to recipient

Completion phase: Period from final state payment to fulfillment of all contract requirements by recipient.

HCD and the Finance Agency Generally Undertake Appropriate Monitoring Procedures During the Disbursement Phase

HCD and the Finance Agency have processes in place to ensure that sponsors meet legal requirements during disbursement of bond funds from propositions 46 and 1C. Table 3 on the following page provides examples of the types of monitoring procedures we reviewed for the five programs we tested during the disbursement phase. The second column in Table 3 provides examples of the monitoring procedures we reviewed and found to be working, whereas the third column identifies the exceptions we found, which we discuss in more detail later in this section.

Table 3
Summary of Testing Results From Our Evaluation of the Two Entities' Monitoring of Five Housing Bond Programs During the Disbursement Phase

ENTITY AND PROGRAM NAME	EXAMPLES OF MONITORING PROCEDURES REVIEWED AND FOUND TO BE WORKING	EXCEPTIONS IDENTIFIED IN TESTING OF MONITORING PROCEDURES
Department of Housing and Community Development (HCD)		
CalHome Program	Ensures that sponsors demonstrate that they have sufficient organization stability and capacity to carry out the activity for which they are requesting funds. To do this, sponsors must have been operating as housing developers or housing program administrators for a minimum of two years prior to the date of application. Requires submittal of plans that describe how sponsors plan to reuse funds they receive as loan repayments from the low- and moderate-income home buyers they have assisted. The funds must be used for the same purpose.	HCD did not follow its procedures or provide appropriate justification when it issued advances exceeding the limit in its standard agreement. HCD did not always receive quarterly status reports that regulations require its sponsors to submit.
Emergency Housing and Assistance Program	Requires sponsors to submit supporting documents, such as contracts and cost estimates, before making disbursements. Ensures that construction began within the initial 12 months of the contract or contract amendment before disbursing funds.	None
Multifamily Housing Program—Supportive Housing Program	Ensures that its sponsors have a recorded regulatory agreement that includes information such as standards for tenant selection and rent schedules in addition to procedures for permitting rent increases. Approves management plans and obtains operating budgets for all its projects before closing on a loan.	None
Workforce Housing Reward Program	Ensures that sponsors are spending funds appropriately by requiring them to submit to HCD documentation supporting their disbursements. Requires sponsors to submit a closeout report that includes notices of completion, certificates of occupancy, or similar documentation demonstrating that the sponsors issued the number of building permits they stated they would in their applications.	None
California Housing Finance Agency (Finance Agency)		
Residential Development Loan Program	Verifies that disbursements for advances or reimbursements under this program are supported by funding requests from sponsors that include a description of the use of funds as required by their loan agreements. Consistently received project status reports from sponsors that inform the Finance Agency of any changes to the initial project proposal, potential schedule delays, and project expenditures to date.	The Finance Agency did not always obtain copies of recorded regulatory agreements to ensure the affordability of properties developed using the bond funds.

Source: Bureau of State Audits-generated based on information from HCD and the Finance Agency.

In selecting which projects to sample within each program, we considered factors such as award amount and whether the project was in the disbursement or completion phase. Given the variability of these factors among the programs, our sample sizes ranged from as small as five projects for the Residential Development Loan Program to as many as 11 projects for the Emergency Housing Program. During our review, as also shown in Table 3, we found that HCD did not always follow its procedures when issuing advances to sponsors receiving CalHome Program bond funds, nor did it consistently collect and review status reports from sponsors. Additionally, the Finance Agency did not always obtain required regulatory agreements from its sponsors for its Residential Development Loan Program.

The length of the disbursement phase varies among programs, depending on the type of assistance the program provides. For example, the disbursement phase can last up to three years for the Workforce Housing Reward Program, but can continue for more than three years for construction projects under the Supportive Housing Program. The disbursement phase begins when HCD or the Finance Agency commits to providing funding and ends when a recipient has received all funds earmarked for an approved loan or grant. Both entities indicated that the purpose of monitoring during this phase is to ensure that sponsors exhibit reasonable progress in meeting goals and that bond funds are provided to sponsors only for allowed costs. For example, HCD requires that the Emergency Housing Program's sponsors provide supporting documentation, such as contracts and cost estimates, before making disbursements. We found that HCD received supporting documents before it disbursed funds to Emergency Housing Program sponsors that had requested fund distributions.

For two programs we reviewed—Workforce Housing Reward and Residential Development Loan—monitoring occurs only during the disbursement phase. For example, during the disbursement phase under the Workforce Housing Reward Program, HCD ensures that sponsors are spending funds appropriately by requiring them to submit documentation supporting their disbursements, and it reviews a closeout report at the completion of a project that contains documents to show that the project was, in fact, completed. As also shown in Table 3, before disbursing bond funds to sponsors of the Residential Development Loan Program, the Finance Agency requires them to have an agreement in place that ensures the future affordability of the property developed under the program. Since the law does not require completion phase monitoring for either of these programs, monitoring ends after the disbursement phase.

For two programs we reviewed—Workforce Housing Reward and Residential Development Loan—monitoring occurs only during the disbursement phase.

Monitoring of Advances Is Particularly Important

HCD disburses funds for its CalHome Program on either an advance basis or a reimbursement basis. In the case of an advance, its standard agreement allows a sponsor a 25 percent advance of awarded funds. The standard agreement states that after the sponsor submits supporting documents for at least two-thirds of an advance, it can receive an additional 25 percent advance. This policy limits the State's risk by requiring sponsors, on an incremental basis, to certify that they are using bond proceeds for allowable purposes.

However, during both our 2007 audit and our current audit, we found that for some of the CalHome Program awards in our sample, HCD lost potential interest earnings because it did not follow its own policy of limiting to 25 percent the bond funds it advanced to sponsors. In our previous review, we reported that for three of the 18 CalHome Program awards we tested, HCD provided sponsors advances that exceeded the 25 percent limit. As a result, it lost the opportunity to earn $42,000 in interest. At that time, we recommended that HCD consider eliminating its override of the 25 percent limit on advances. In its response to our recommendation, HCD stated that in some cases 25 percent is not sufficient to provide the cash flow needed to support the rate at which sponsors make loans and that in these cases a limitation on advances could result in missed home purchase opportunities. However, HCD also stated its intent to establish clear procedures to guide staff in evaluating circumstances under which an advance above the 25 percent limitation may be appropriate, as well as documenting the justification for exceeding this limit.

For two of the 10 awards for the CalHome Program that we tested during this current audit, HCD did not provide appropriate justification when it issued advances exceeding the 25 percent limit.

Subsequent to our 2007 audit, HCD established criteria for issuing advances of more than 25 percent. However, for two of the 10 awards for the CalHome Program that we tested during this current audit, HCD did not provide appropriate justification when it issued advances exceeding the limit. Based on these two cases, we calculated a potential interest loss to the State of as much as $9,385. HCD indicated that its staff did not follow the new procedures in these cases and asserted that it plans to conduct training to ensure their appropriate application in the future.

Periodic Reports and Other Documentation Need to Be Monitored Regularly

Depending on the length of the disbursement phase, many of the housing bond programs HCD and the Finance Agency administer require the submission of periodic reports. For example, the CalHome Program's regulations require that sponsors submit quarterly performance reports to HCD, which it uses to assess the status of sponsor activities. These reports include the current status of program activity, future planned activities, problems or delays encountered and the courses of action to be taken to address them, and the actions taken to meet expenditure deadlines. However, HCD's files did not contain any of the required quarterly reports for five of the 10 projects we tested. In addition, we could not locate 13 of 31 quarterly reports that sponsors should have submitted for the remaining five projects we reviewed. In these instances, HCD could not demonstrate that it had received and reviewed these reports. According to the CalHome program manager, staff are aware that they should monitor these reports, and after we pointed out this problem to HCD, it reminded the sponsors of the importance of sending in quarterly reports. The program manager explained that beginning in June 2009, the program uses a quarterly report log sheet on which staff record the date they received and reviewed the quarterly reports, which will assist the program manager in monitoring them.

The Finance Agency did not always ensure that its sponsors have regulatory agreements in place, which provide assurance that the developments being built using funds from the Residential Development Loan Program remain affordable to low- and moderate-income households.

We also found that the Finance Agency did not always ensure that its sponsors have regulatory agreements in place. These agreements provide assurance that the developments being built using funds from the Residential Development Loan Program remain affordable to low- and moderate-income households. As part of the loan agreement, the Finance Agency requires that the sponsor record a regulatory agreement certifying the project's affordability before the sponsor may request funds. We reviewed all 12 Residential Development Loan Program sponsors to determine whether they had submitted regulatory agreements to the Finance Agency. At the time of our review, three sponsors had not yet requested funds and did not need to submit regulatory agreements. Of the remaining nine, the Finance Agency was unable to locate the regulatory agreements for three sponsors, and the regulatory agreements for two more awards were dated after the sponsors had received bond funds. According to the program manager, the loan agreements did not specifically require the sponsors to send the Finance Agency copies of the recorded agreements. However, the Finance Agency plans to amend the loan agreements to impose this requirement so that it can ensure that it obtains the recorded copies of regulatory agreements before making any disbursements in the future. By not obtaining signed copies of these agreements, the Finance Agency has no assurance that the sponsor is using the property for the intended purposes of the program.

HCD Needs to Improve Its Efforts to Monitor During the Completion Phase

We reviewed the completion phase monitoring for three programs: CalHome, Emergency Housing, and Supportive Housing. All three had processes in place that should assist in ensuring compliance during the completion phase. In fact, HCD has improved its processes for the CalHome and Emergency Housing programs, which our 2007 audit identified as having weak or nonexistent monitoring during the completion phase. Both programs now have monitoring procedures in place to ensure that sponsors are using bond funds to help their intended populations. However, HCD imposed travel restrictions on its staff in response to the State's budget difficulties, which caused it to scale back on the number of monitoring site visits it planned to make. We also found some instances in which HCD did not promptly communicate its findings made during site visits to housing sponsors.

Monitoring during the completion phase, which extends from when HCD has finished disbursing funds for a loan or grant to the completion of contractual requirements, varies greatly depending on the type of housing assistance involved. For the Emergency Housing Program, the completion phase is five years for small rehabilitation loans, seven years for substantial rehabilitation, and 10 years for acquisition and rehabilitation or new construction. In contrast, the completion phase for the Supportive Housing Program can last up to 55 years.

To better target its monitoring efforts, HCD performed risk assessments of the CalHome and Emergency Housing programs' sponsors and attempted to focus its on-site visits on high-risk sponsors.

In our September 2007 audit, we reported that HCD's completion phase monitoring of the CalHome and Emergency Housing programs was weak or nonexistent. In December 2007 and February 2008, respectively, HCD adopted monitoring policies and procedures for each program that include risk assessment processes to identify those sponsors needing an on-site monitoring visit and requirements the sponsors must follow to address concerns identified during monitoring visits. For its CalHome Program, HCD has written procedures outlining staff responsibilities before, during, and after an on-site monitoring visit. To better target its monitoring efforts, HCD performed risk assessments of the CalHome and Emergency Housing programs' sponsors and attempted to focus its on-site visits on high-risk sponsors.

According to its policies, on-site monitoring is a critical component of HCD's monitoring plans. On-site monitoring allows it to confirm information provided by sponsors, ensure that sponsor expenditures were for eligible purposes, and verify that the number of housing units claimed by sponsors has actually been produced. Generally, program staff complete a checklist of the required elements of the program and describe their findings in a letter. Additionally, HCD has set annual goals for the number of on-site visits to perform for each of the two programs.

However, HCD has been unable to meet these annual goals because it needed to scale back its site visit activities for several reasons. In July 2008, as a result of the delay in enacting the fiscal year 2008–09 budget, HCD limited travel to critical activities and required all travel to be preapproved through its director's office. Also, in December 2008 Finance suspended bond activities, which deferred bond-related disbursements, except for necessary administrative costs. Although Finance continued the suspension in January 2009, it allowed departments to proceed with necessary administrative expenses, including travel costs, for up to a maximum specified amount as approved by Finance. HCD stated, however, that the amount Finance approved through June of 2009 was not sufficient to cover its planned administrative costs. As a result, HCD indicated that it limited its routine monitoring activities to those it identified as critical.

The amount of monitoring-related travel HCD allowed varied by program. For example, it told us that during fiscal year 2008–09, it performed 17 of the 60 site visits it had originally planned to make to Emergency Housing Program sponsors. HCD indicated that it generally limited its on-site visits for this program to sites within a one-day travel distance from the Sacramento office. HCD also indicated that it attempted to focus its visits on the Emergency Housing Program sponsors that it assessed as higher risk. However, as of May 2009, although HCD had visited about 10 of the sponsors it identified as medium risk, it had not performed an on-site visit of the three it identified as high risk for this program. Ultimately, HCD told us that it completed the site visits for these projects in late September 2009.

HCD also completed a risk assessment of its CalHome Program sponsors. However, as of June 2009 it had not performed any on-site visits since June 2008. According to HCD, sponsors of its CalHome Program are responsible for ensuring that only eligible households receive financial assistance. It also stated that physical inspections are not as essential for this program because funds are eventually disbursed as loans to individuals, as opposed to payments for a particular project. Additionally, HCD stated that while it is important to ensure tenant eligibility, HCD considers on-site monitoring for the CalHome Program as noncritical. Nevertheless, the CalHome Program's monitoring procedures state that on-site monitoring is a critical component of any monitoring plan and that on-site monitoring allows HCD to verify the information provided in the borrower summaries and to ensure that all expenses have been for eligible purposes. In addition, its monitoring checklists for owner-occupied rehabilitation projects under the CalHome Program indicate that, if selected for an on-site inspection, the monitor should perform a walk-through of the property.

As of June 2009 HCD had not performed any on-site visits since June 2008, even though two of the projects on the CalHome Program's risk assessment scored over 45 points, with 50 points indicating the highest level of risk.

We believe that HCD, similar to its handling of the Emergency Housing Program, should focus its monitoring efforts for its CalHome Program on higher risk sponsors. For example, two of the unmonitored projects on the CalHome Program's risk assessment scored over 45 points, with 50 points indicating the highest level of risk. By failing to monitor at least the higher risk sponsors, HCD cannot ensure that sponsors use funds in accordance with housing bond requirements or that the program is benefiting the intended populations.

In our review of on-site visits it performed before June 2008 for the CalHome Program, we found that HCD did not always promptly communicate findings and concerns to sponsors. HCD's CalHome Program monitoring procedures require that it communicate any concerns, findings, and suggestions for correction resulting from an on-site visit to the sponsor in writing within 30 days of the visit. Of the four on-site visits we reviewed in which it had concerns or findings, HCD was unable to provide us with its written communication to one sponsor. For two other sponsors, it sent notices four months after the 30-day deadline. According to the program manager, delays in sending the written communications to the sponsors resulted from a change of management within the program.

In addition, although its procedures for the CalHome Program state that the sponsor has 30 days to provide a response to site visit findings, HCD was unable to provide us with two of the sponsors' responses. The program manager stated that the lack of sponsor responses in the files might be the result of poor file management. HCD has since provided e-mail correspondence indicating that it had been communicating with these sponsors. Nevertheless, because it has not ensured that it provides sponsors with prompt written communications about the issues it identifies during on-site monitoring visits or ensured that sponsors provide appropriate responses, HCD cannot be certain that sponsors are taking timely and appropriate corrective actions.

For the multifamily housing programs, which include the Supportive Housing Program and other projects that involve long-term loans to sponsors, HCD assigned responsibility for monitoring compliance with contract terms to its Asset Management and Compliance Section (Compliance Section) under its Division of Financial Assistance. As previously mentioned, the monitoring activities for this program can last up to 55 years. According to HCD, the Compliance Section provides oversight to ensure that program housing continues to be used for its intended purpose, loan or grant conditions are met, housing remains safe and financially stable, and loan repayments are made as required. According to the chief of the Compliance Section, staff perform on-site visits of the programs it is responsible for on a three-year cycle following the close of a loan. The chief also acknowledged that the Compliance Section should have monitored three sponsors under its Supportive Housing Program since July 2008 if it were following its three-year cycle. Although the chief indicated that HCD's travel restrictions do not preclude the Compliance Section from performing on-site visits of critical projects, HCD did not identify any sponsors as having a critical need for a site visit; thus, it did not perform any on-site visits during fiscal year 2008–09.

Although the chief indicated that HCD's travel restrictions do not preclude the Compliance Section from performing on-site visits of critical projects, HCD did not identify any such sponsors as having a critical need for a site visit; thus, it did not perform any on-site visits during fiscal year 2008–09 for the Supportive Housing Program.

When scheduled site visits are not made, HCD has less assurance that the occupants of projects funded by the Supportive Housing Program meet minimum eligibility requirements.

Ultimately, the assistant deputy director for program policy told us that management gave its approval, in early September 2009, for the Compliance Section to resume its site visits. However, the deputy director also indicated that, as part of HCD's approval to resume site visits, the Compliance Section is expected to revise its site visit policy from reviewing all projects once every three years to using a risk-based approach that prioritizes site visits based on identified risk factors.

HCD Has Not Yet Completed Its Verification of Data Transferred to a New System

During our September 2007 audit, we found that HCD lacked sufficient internal controls over its information technology system. In accordance with generally accepted auditing standards, we discussed this matter in a separate letter dated September 17, 2007, rather than include it in our 2007 report. Although this weakness did not have a bearing on the testing performed during this audit or our 2007 audit, it could affect the accuracy and completeness of future information reported by HCD.

Specifically, HCD did not ensure the accuracy and completeness of the data converted into its Consolidated Automated Program Enterprise System (CAPES), which it uses to administer and manage various housing programs. When implementing the system, HCD did not include in its conversion plan a method for verifying that converted data transferred into the new system were accurate and complete. According to the project manager of major information technology projects, HCD performed spot checks of the converted data. However, HCD's testing of the converted data was not documented or reviewed. As a result, HCD has little assurance that CAPES contains data that are accurate or complete. Additionally, because HCD used an informal, undocumented process for verifying converted data, it did not comply with the *State Administrative Manual*, Section 5335.1, which states that the accuracy and completeness of data maintained within information systems should be a management concern and that controls should be established to ensure that the data entered into and stored in a department's database are accurate and complete.

HCD did not ensure the accuracy and completeness of the data converted into its Consolidated Automated Program Enterprise System, which it uses to administer and manage various housing programs.

Furthermore, HCD did not follow best practices from the California Office of Systems Integration and the Control Objectives for Information and Related Technologies (COBIT) framework for information technology processes published by the IT Governance Institute. These best practices prescribe a data conversion plan that details how converted data will be validated when performing system implementation. State best practices also dictate that converted data should be validated prior to being loaded into the production system, while COBIT states that original and converted data should be compared for completeness and integrity.

On August 27, 2008, in its one-year response to our management letter, HCD reported that it expected all converted data would be validated and, where necessary, corrected by April 2009. However, when we inquired about the status of its efforts as part of our current audit, HCD indicated that it does not expect to complete the process until March 2010. To its credit, HCD developed the CAPES Data Clean-Up Plan to organize and track this effort. The plan identifies the data that needs to be checked, the source documents that will be used to verify the data, how the verification will be documented, and a timeline for completion.

Although HCD has made progress in its cleanup efforts, we were unable to verify the percentage of completion because the method the department uses to track its progress did not allow us to do so. In particular, the documentation HCD has provided us thus far does not clearly indicate which records and data elements have been checked and which ones remain to be checked. Additionally, the documentation does not indicate the individual responsible for the data validation or the individual who reviewed the work.

Certain Programs Funded by Proposition 1C Are Not Subject to Periodic Audits by the Bureau of State Audits

As indicated in our Scope and Methodology section, statutes require the Bureau of State Audits (bureau) to conduct periodic audits of housing bond activities to ensure that these funds are awarded in a manner that is timely and consistent with legal requirements, as well as to ensure that recipients use the funds in compliance with the law. Although a statute subjects all $2.1 billion authorized under Proposition 46 to an audit by the bureau, the statutes concerning Proposition 1C require the bureau to conduct periodic audits of only $1.5 billion, or 53 percent, of the $2.85 billion in bonds that were authorized. As we discuss in the Introduction, Proposition 1C does not require the bureau to conduct periodic audits of three programs under Proposition 1C—the Transit-Oriented Development Implementation Program; the Regional Planning, Housing, and Infill Incentive Account; and the Housing Urban-Suburban-Rural Parks Account—that

Neither Proposition 1C nor subsequent legislation requires the bureau to conduct periodic audits of three programs that constitute 47 percent of the $2.85 billion in bonds authorized under Proposition 1C.

constitute the remaining 47 percent. A change in the statute would be necessary for the bureau to perform periodic audits of these three programs.

Recommendations

HCD should continue its efforts to monitor recipients of housing bond funds by doing the following:

- Follow its procedures on restrictions of bond fund advances that exceed 25 percent of the total award under the CalHome Program.
- Ensure that it receives and reviews required status reports from recipients of its CalHome Program.
- When practical, adopt a risk-based, on-site monitoring approach for its CalHome and Supportive Housing programs similar to the monitoring methodology used for the Emergency Housing Program.
- Promptly communicate concerns and findings identified during on-site visits conducted for its CalHome Program and ensure that recipients provide a timely response to the concerns and findings.

To ensure that sponsors are using properties for the intended purposes of the Residential Development Loan Program, the Finance Agency should obtain signed copies of recorded regulatory agreements before disbursing funds to them.

To ensure that data maintained in CAPES are accurate and complete, HCD should complete its review of the accuracy of the data transferred to CAPES. HCD should also ensure that its cleanup efforts are thoroughly documented and retained for future reference.

If the Legislature believes that the bureau should perform periodic reviews of the bond programs not currently included in the audit requirements under Proposition 1C, it should propose legislation to require the bureau to do so.

We conducted this review under the authority vested in the California State Auditor by Section 8543 et seq. of the California Government Code and according to generally accepted government auditing standards. We limited our review to those areas specified in the audit scope section of the report.

Respectfully submitted,

Elaine M. Howle

ELAINE M. HOWLE, CPA
State Auditor

Date: November 10, 2009

Staff: Denise L. Vose, CPA, Audit Principal
Nicholas Kolitsos, MBA
Arthur Meyer
Angela Owens, MPPA
Benjamin W. Wolfgram, ACDA
Jordan Wright, MPA

Legal Counsel: Scott A. Baxter, JD

For questions regarding the contents of this report, please contact
Margarita Fernández, Chief of Public Affairs, at 916.445.0255.

Appendix

PROGRAMS FUNDED BY THE HOUSING AND EMERGENCY SHELTER TRUST FUND ACTS OF 2002 AND 2006

Table A presents key details of programs funded by the Housing and Emergency Shelter Trust Fund Act of 2002 (Proposition 46) and the Housing and Emergency Shelter Trust Fund Act of 2006 (Proposition 1C). The programs are categorized into five core areas: multifamily housing programs, home ownership programs, farmworker housing programs, development programs, and other programs. For each program, the table lists the year it was established, a brief description, and the program's allocation under each proposition as of December 31, 2008; the agency directly managing the program is also indicated.

The Department of Housing and Community Development (HCD) directly administers 16 of the 23 programs funded under Proposition 46, while the California Housing Finance Agency (Finance Agency) manages the other seven programs. For the 13 Proposition 1C programs, HCD is responsible for directly managing 12 programs and the Finance Agency manages one.

Table A
Key Details for Programs Funded by the Housing and Emergency Shelter Trust Fund Acts of 2002 and 2006

CORE AREA AND PROGRAM NAME	YEAR PROGRAM ESTABLISHED	DESCRIPTION OF PROGRAM	PROPOSITION 46* ALLOCATION	PROPOSITION 1C† ALLOCATION
Multifamily Housing Programs				
Downtown Rebound Program	2000	Loans and/or grants for rental housing development projects located within one-quarter mile of an existing or planned major transit node. Funding priority is given to projects developed within walking distance of schools; major employment centers; or public amenities, including shopping, parks, and major entertainment venues.	$15,000,000	
Exterior Accessibility Grants for Renters Program	2002	Grants for exterior modification to rental housing to accommodate low-income renters with disabilities.	5,000,000	
Local Housing Trust Fund Matching Grant Program	2002	Matching grants to local housing trust funds that provide loans for the construction of rental housing projects or units within rental housing projects for very low-income persons and families earning less than 60 percent of the area median income.	25,000,000	
Multifamily Housing Program—General	1999	Deferred-payment loans for the development and construction of new, and the rehabilitation or acquisition and rehabilitation of existing, transitional, or rental housing developments.	797,598,695	$345,000,000
Multifamily Housing Program—Governor's Homeless Initiative	2005	Interagency effort among the Department of Housing and Community Development (HCD), the California Housing Finance Agency, and the Department of Mental Health aimed at reducing the number of persons with severe mental illness who are chronically homeless by developing permanent supportive housing.	40,000,000	

continued on next page . . .

Agency directly managing program: = Department of Housing and Community Development = California Housing Finance Agency

CORE AREA AND PROGRAM NAME	YEAR PROGRAM ESTABLISHED	DESCRIPTION OF PROGRAM	PROPOSITION 46* ALLOCATION	PROPOSITION 1C† ALLOCATION
Multifamily Housing Program—Homeless Youth	2002	Loans to facilitate and support the development and operation of housing for homeless youth.		50,000,000
Multifamily Housing Program—Nonresidential Space for Supportive Services	2002	Grants for nonresidential space for supportive services providing job training, health services, and child care within or immediately proximate to projects funded by other multifamily housing programs.	$20,000,000	
Multifamily Housing Program—Supportive Housing Program	2002	Loans for supportive housing for individuals and households moving from emergency shelters or transitional housing or those at risk of homelessness. Loans are used for rental units linked to supportive services where occupancy is restricted to households that include a disabled adult and are homeless or at risk of homelessness.	195,000,000	195,000,000
Preservation Opportunity Program	2002	Loans for at-risk units that will likely convert to market-rate housing.	12,401,305	
Residential Development Loan Program	2005	Low-interest rate loans to housing sponsors for site acquisition and predevelopment expenses related to affordable infill owner-occupied housing developments.	44,048,000	
Subtotals			**$1,154,048,000**	**$590,000,000**
Home Ownership Programs				
Building Equity and Growth in Neighborhoods	2002	Grants to cities, counties, or cities and counties to be used for down payment assistance to first-time low- and moderate-income home buyers purchasing newly constructed homes within a Building Equity and Growth in Neighborhoods project.	$75,000,000	$125,000,000
CalHome Program	2000	Grants and loans to private nonprofit and local government agencies that aid households with low and very low incomes. Grants are used for first-time home buyer down-payment assistance, home rehabilitation, home buyer counseling, self-help mortgage assistance programs, or technical assistance for self-help home ownership. Loan funds may be used for purchase of real property, site development, predevelopment and construction period expenses incurred on home ownership development projects, and permanent financing for mutual housing or cooperative developments.	115,000,000	290,000,000
California Self-Help Housing Program	1978	Grants to public entities and private nonprofit entities to provide assistance to persons and families of low to moderate income who are owner-builders or self-help rehabilitators.	10,000,000	10,000,000
California Homebuyer's Downpayment Assistance Program	2000	Down-payment assistance, including deferred-payment low-interest loans to reduce principal and interest payments and make financing affordable for first-time low- to moderate-income home buyers.	152,152,000	200,000,000
Extra Credit Teacher Home Purchase Program	2000	Federal mortgage credit certificates and reduced-interest loans funded by mortgage revenue bonds to eligible teachers, principals, vice principals, assistant principals, and classified employees who agree to teach or provide administration or service in high-priority schools.	25,000,000	
Homebuyer Downpayment Assistance Program—School Facility Fee	2002	Assistance to qualified first-time home buyers in the form of a partial or full rebate of the school facility fees on affordable housing.	50,000,000	
Homeownership in Revitalization Areas Program	2002	Down-payment assistance to low- and moderate-income first-time home buyers who are purchasing a residence in a community revitalization area as documented by a nonprofit organization. Down-payment assistance may include loans to provide deferred-payment subordinate loans to borrowers to be used for down payments or closing costs, totaling up to 6 percent of a home's purchase price.	9,100,000	
Subtotals			**$436,252,000**	**$625,000,000**

Agency directly managing program: [blue] = Department of Housing and Community Development [green] = California Housing Finance Agency

CORE AREA AND PROGRAM NAME	YEAR PROGRAM ESTABLISHED	DESCRIPTION OF PROGRAM	PROPOSITION 46* ALLOCATION	PROPOSITION 1C† ALLOCATION
Farmworker Housing Programs‡				
Joe Serna, Jr. Farmworker Housing Grant Program—General	1977	Grants and loans for construction or rehabilitation of housing for agricultural employees and their families. Also includes loans and grants for the acquisition of manufactured housing as part of a program to address and remedy the impacts of current and potential displacement of farmworker families.	$155,000,000	$135,000,000
Joe Serna, Jr. Farmworker Housing Grant Program—Migrant Housing	2001	Projects that serve migratory agricultural workers, including grant funds reserved for development of housing for migrant farmworkers.	25,000,000	
Joe Serna, Jr. Farmworker Housing Grant Program—Wellness Program	2000	Health services to achieve the goal of advancing comprehensive strategies for improving the health status of agricultural workers and their families.	20,000,000	
Subtotals			**$200,000,000**	**$135,000,000**
Development Programs§				
Regional Planning, Housing, and Infill Incentive Account	2006	Legislation in 2007 established the Infill Incentive Grant Program of 2007 and requires that funds from the account be used for selected capital improvement projects related to qualifying infill projects or areas. This legislation appropriated $240 million of the $850 million to be used for this program in fiscal year 2007–08. The same legislation established a second program—the California Recycle Underutilized Sites Program—to provide grants and loans to clean up environmentally contaminated sites that also promotes infill residential and mixed-used development, consistent with regional and local land use plans. It also designated the California Pollution Control Financing Authority under the State Treasurer's Office as the administering agency of the loans and grants for this program. The legislation appropriated $60 million of the $850 million to be used for this program in fiscal year 2007–08.		$850,000,000
Housing Urban-Suburban-and Rural Parks Account	2006	Legislation in 2008 established the Housing-Related Parks Program and requires that funds from the account be used to provide grants for the creation, development, or rehabilitation of park and recreation facilities to cities, counties, and cities and counties that meet certain criteria.		200,000,000
Transit-Oriented Development Implementation Program	2006	Assistance to cities, counties, cities and counties, transit agencies, and developers to establish higher-density uses within close proximity to transit stations.		300,000,000
Subtotal				**$1,350,000,000**
Other Programs				
Affordable Housing Innovation Fund	2006	Grants and loans to entities that develop, own, invest in, or make loans for affordable housing. Also used to create pilot programs to demonstrate innovative, cost-saving approaches to creating or preserving affordable housing. Legislation in 2007 established several programs, including the Affordable Housing Revolving Development and Acquisition Program to use money from this fund to provide loans to applicants to purchase real property for the development or preservation of housing affordable to low-income households.		$100,000,000
Code Enforcement Incentive Program	2000	Grants to increase staffing or capital expenditures dedicated to local building code enforcement efforts.	$5,000,000	
Emergency Housing and Assistance Program	1993	Capital development grants for programs such as acquisition, leasing, construction, or rehabilitation of sites for emergency shelter and transitional housing for homeless persons.	195,000,000	50,000,000

continued on next page . . .

Agency directly managing program: = Department of Housing and Community Development = California Housing Finance Agency

CORE AREA AND PROGRAM NAME	YEAR PROGRAM ESTABLISHED	DESCRIPTION OF PROGRAM	PROPOSITION 46* ALLOCATION	PROPOSITION 1C† ALLOCATION
Workforce Housing Reward Program	2002	Capital grants to provide local assistance for the construction or acquisition of capital assets for cities, counties, and cities and counties that provide land use approval to affordable housing developments. Also provides $25 million of the $100 million to the Jobs-Housing Balance Incentive Grant Program, which provides grants to encourage construction of housing in those areas that have experienced the greatest increase in job growth but have not kept pace with necessary housing and to attract new business and jobs to areas that lack a sufficient employment base.	100,000,000	
Mortgage Guaranty Insurance Program	1993	Bond and loan insurance to facilitate financing for low- and moderate-income housing by reducing risk to the lender.	9,700,000	
Subtotals			**$309,700,000**	**$150,000,000**
Totals			**$2,100,000,000**	**$2,850,000,000**

Agency directly managing program: = Department of Housing and Community Development = California Housing Finance Agency

Sources: Health and Safety Code, Division 31, parts 11 and 12, and HCD's *Cumulative Proposition 46 Bond Awards Report Through December 31, 2008*.

Notes: The amounts shown in the funding columns for Proposition 46 represent funding available to the programs on December 31, 2008, and as a result may not agree with the original funding levels for the programs presented in the law. The following programs received additional funding from other housing bond programs due to reversions required by statute, transfers from existing programs to new programs, or program discontinuation:

	Original Allocation by Proposition 46 in 2002 (in Millions)	Change (in Millions)	Current Balance (in Millions)
California Homebuyer's Downpayment Assistance Program	$117.5	$34.7	$152.2
Downtown Rebound Program	0.0	15.0	15.0
Multifamily Housing Program—Governor's Homeless Initiative	0.0	40.0	40.0
Multifamily Housing Program—General	800.0	(2.4)	797.6
Residential Development Loan Program	0.0	44.0	44.0
Preservation Programs	50.0	(37.6)	12.4

In addition, the California Homebuyer's Downpayment Assistance Program received an additional $100 million from the Residential Development Loan Program under Proposition 1C. This program's total allocation from Proposition 1C is currently $200 million.

* Housing and Emergency Shelter Trust Fund Act of 2002.

† Housing and Emergency Shelter Trust Fund Act of 2006.

‡ The Proposition 1C bond act allows the HCD to use the Joe Serna, Jr. Farmworker funds on any of the Joe Serna programs listed under Farmworker Housing Programs; however, HCD has chosen to use the funds for the general program exclusively.

§ Development programs are not subject to audit by the Bureau of State Audits.

(Agency response provided as text only.)

Business, Transportation and Housing Agency
980 9th Street, Suite 2450
Sacramento, CA 95814-2719

October 23, 2009

Elaine M. Howle, State Auditor*
Bureau of State Audits
555 Capitol Mall, Suite 300
Sacramento, CA 95814

Dear Ms. Howle:

Attached please find responses from the Department of Housing and Community Development and the California Housing Finance Agency to your draft audit report *Department of Housing and Community Development: Housing Bond Funds Generally Have Been Awarded Promptly and in Compliance With Law, but Monitoring Continues to Need Improvement* (#2009-037). Thank you for allowing the Departments and the Business, Transportation and Housing Agency (Agency) the opportunity to respond to the report.

As noted in their responses, the Departments concur with the findings noted in the report, and either have implemented or are in the process of implementing the recommendations. We appreciate your identification of opportunities for improvement and your recommendation for best practices the Departments can follow.

If you need additional information regarding the Departments' responses, please do not hesitate to contact Michael Tritz, Agency Deputy Secretary for Audits and Performance Improvement, at (916) 324-7517.

Sincerely,

(Signed by: Michael R. Tritz for)

DALE E. BONNER
Secretary

Attachments

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* California State Auditor's comment appears on page 47.

Department of Housing and Community Development
Office of the Director
1800 Third Street, Room 450
Sacramento, CA 95811

October 23, 2009

Mr. Dale E. Bonner, Secretary
Business, Transportation and Housing Agency
980 Ninth Street, Suite 2450
Sacramento, CA 95814

Dear Secretary Bonner:

The Department of Housing and Community Development (Department) was pleased to assist the Bureau of State Audits (Bureau) in its periodic audit of the Proposition 46 and Proposition 1C housing bond programs. The Department continues in its efforts to improve processes that ensure bond funds continue to be awarded in a timely manner that provides affordable housing and infrastructure. The Department is taking the necessary corrective actions to ensure compliance. In several cases, as reflected below, the appropriate corrective action has already been implemented:

1. The Bureau of State Audits recommended that HCD should continue its efforts to monitor recipients of housing bond funds by doing the following:

- *Follow its procedures on restrictions of bond fund advances over 25 percent under the CalHOME Program.*

Department's Response and Corrective Action Plan:

The ability for CalHOME to grant a funding advance in excess of 25 percent under special circumstances is important to mitigate risks to participants (occupants) who might otherwise lose an opportunity to own and occupy a home. The risk of lost interest is outweighed by the benefit of supplying affordable housing to low income participants at the lowest possible rate. Therefore, CalHOME developed and implemented a procedure for granting advances in excess of 25 percent that requires the following: substantiation from the recipient; addition of the request to the tracking report; and review and approval by the manager. The request is then documented, processed and filed in the recipient's file. The Department believes that this procedure ensures that the appropriate controls are in place.

Through this Bureau audit, it was determined that provisions of the Standard Agreement (contract) used for CalHOME grants conflict with the Department's policy to allow funding advances in excess of 25 percent under special circumstances. The Department is revising the Standard Agreement to address this problem and will have completed this effort by January 1, 2010.

Further, the two instances of noncompliance identified by the Bureau through this audit were traced back to two staff members who no longer work in the Department. To ensure that subsequent infractions of the procedure do not occur, the Department has reissued the procedure to all CalHOME staff members.

Mr. Dale E. Bonner, Secretary
Page 2

- *Ensure that it receives and reviews required status reports from sponsors of its CalHome Program.*

Department's Response and Corrective Action Plan:

Status reports are due 30 days after the end of every quarter. As contractors receive an award, they are added to a quarterly report tracking log (previously, staff kept their own log; it will now be centralized). If reports are late, staff call or email the contractor and note on the log who called, who the contact was, date called and result. The log is reviewed periodically by the manager and follow-ups are performed as necessary.

Prior to the Bureau's most recent visit, staff routinely reviewed and filed these status reports. However, as the files were recently reviewed by the Bureau auditors, the CalHOME manager found a folder of quarterly reviews that had been left unfiled by former staff. Consequently, the manager has reviewed the status report process with staff and has commenced routine periodic reviews of the centralized tracking log to ensure that the reports are received in a timely manner and filed appropriately. This will be documented on the log and in the individual contract folders.

- *When practical, adopt a risk-based, on-site monitoring approach for its CalHome and Supportive Housing programs similar to the monitoring methodology used for the Emergency Housing Program.*

Department's Response and Corrective Action Plan

The Department has adopted a risk-based, on-site monitoring approach for its CalHome and Supportive Housing programs similar to the monitoring methodology used for the Emergency Housing and Assistance Program-Capital Development (EHAP-CD). The Department has also re-examined and re-communicated its travel expenditure policy to support field visits to conduct site monitoring. 1

- *Promptly communicate its concerns and findings identified during on-site visits for its CalHome Program.*

Department's Response and Corrective Action Plan:

The Department concurs that it is important to communicate concerns and findings identified to the contractors. There has been a longstanding, documented process for such communication, which includes that such letters are required to be prepared by CalHOME staff within a defined timeframe. However, during a change in management these letters were inadvertently not approved or sent to the contractors. The current manager is developing a centralized tracking log for the site monitoring that will include the name of the recipient (contractor) and dates of the following: site visit and completion, letter of findings, and clearance of findings. Original documentation will be stored in the contractor's file. The tracking log will be completed by October 31, 2009, and will ensure that, in the event of any future management changes, the process will be followed.

Additionally, the EHAP-CD program is currently developing a report in the Consolidated Automated Program Enterprise System (CAPES) that will provide dates (proposed and actual) for site visits, letters of findings, and clearance of findings. This will be made available to all programs by April 1, 2010.

Mr. Dale E. Bonner, Secretary
Page 3

2. *Regarding the Department's CAPES, the Bureau of State Audits recommended as follows:*

- *To ensure that data maintained in CAPES are accurate and complete, HCD should complete its review of the accuracy of the data transferred to CAPES. HCD should also ensure that its cleanup efforts are thoroughly documented and retained for future reference.*

Department's Response and Corrective Action Plan

The Department concurs in the necessity to complete its review of the accuracy of the data transferred to CAPES. Due to time and staffing constraints, it was not possible to check all data prior to the conversion process, as would have been ideal. However, subsequently, the Department developed a comprehensive cleanup plan that not only encompassed the converted data mentioned in the previous report, but also the data entered into CAPES after the May 2007 implementation. However, the State's fiscal situation, which has resulted in continuing staffing limitations for the Department, has impeded the Department's efforts to complete the entire cleanup process prior to this audit by the Bureau. The Department will finish the cleanup of the CAPES data by March 2010, and ensure that thorough documentation of the cleanup efforts will be available at the next periodic visit by the Bureau.

Sincerely,

(Signed by: Elliott Mandell for)

Lynn L. Jacobs
Director

California Housing Finance Agency
Sacramento Headquarters
P.O. Box 4034
Sacramento, CA 95812

October 20, 2009

Mr. Dale Bonner, Secretary
Business, Transportation & Housing Agency
980 9th Street, Suite 2450
Sacramento, CA 95814-2719

Re: BUREAU OF STATE AUDITS REVIEW OF PROP 46/PROP 1C FUNDS

Dear Secretary Bonner:

The Bureau of State Audits (BSA) has completed its most recent review of the Housing and Emergency Shelter Trust Fund Acts of 2002 (Proposition 46 funds) and 2006 (Proposition 1C). The final report contains a single recommendation related to the California Housing Finance Agency (CalHFA) administration of these funds.

Specifically, the BSA found that in one program administered by CalHFA, the Residential Development Loan Program (RDLP), CalHFA did not always obtain recorded copies of regulatory agreements from the localities prior to disbursing funds to them. By not obtaining copies of these agreements, BSA expressed concern that CalHFA could not ensure that sponsors were using properties in a manner consistent with the intent of the program. While RDLP Loan Agreements do, in fact, require a locality to record a Regulatory Agreement against the subject property prior to any funding disbursements, CalHFA had not required a recorded copy to be sent to the agency. As a result, a number of files lacked this particular documentation.

CalHFA agrees this is an important safeguard that should be implemented. CalHFA has already contacted all awardees requesting this documentation and have amended our monitoring procedures to including requiring a copy of the recorded Regulatory Agreement prior to any future funding disbursements. The majority of the files are now complete, and we expect full compliance from the remaining participants shortly. As part of our efforts, we have suspended any further funding disbursement to these localities until they comply with this requirement.

CalHFA employees are extremely dedicated to ensuring these funds are used as efficiently and effectively as possible. We especially wish to thank the BSA for its diligence and thoroughness in completing this audit. In particular, Nick Kolitsos, Angela Owens, AJ Meyer and Ben Wolfgram were not only courteous, but professional and efficient in handling their audit responsibilities.

Mr. Dale Bonner -2- October 21, 2009

I look forward to continuing our successful participating in these programs. Please contact me at (916) 324-4640 if there are any questions regarding this audit.

Sincerely,

(Signed by: L. Steven Spears)

L. Steven Spears
Acting Executive Director

Comment

CALIFORNIA STATE AUDITOR'S COMMENT ON THE RESPONSE FROM THE DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT

To provide clarity and perspective, we are commenting on the response to our report from the Department of Housing and Community Development (HCD). The number below corresponds with the number we have placed in the margin of HCD's response.

1 While we appreciate the speed with which HCD adopted our recommendation, HCD did not have a risk-based, on-site monitoring approach for its Supportive Housing Program until we brought our concern to its attention in September 2009. Furthermore, as we discuss on page 31 of the report, HCD completed a risk assessment of its CalHome Program sponsors; however, as of June 2009 it had not performed any on-site visits since June 2008.

cc: Members of the Legislature
Office of the Lieutenant Governor
Milton Marks Commission on California State
Government Organization and Economy
Department of Finance
Attorney General
State Controller
State Treasurer
Legislative Analyst
Senate Office of Research
California Research Bureau
Capitol Press