

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

REPORT NUMBER 2009-037, NOVEMBER 2009

Department of Housing and Community Development's and California Housing Finance Agency's responses as of November 2009

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.

The California Health and Safety Code requires the Bureau of State Audits (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.

Finding #1: HCD and the Finance Agency generally undertake appropriate monitoring procedures during the disbursement phase.

For disbursement of housing bond awards, both agencies generally have processes in place to ensure that recipients meet legal requirements. However, HCD did not always follow its procedures when issuing advances to sponsors receiving CalHome Program bond funds. 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 that developments being built using funds from the Residential Development Loan Program remain affordable to low- and moderate-income households.

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.*

We recommended that HCD follow its procedures on restrictions of bond fund advances that exceed 25 percent of the total award under the CalHome Program. In addition, HCD should ensure that it receives and reviews required status reports from recipients of funds under its CalHome Program. We also recommended that the Finance Agency obtain signed copies of recorded regulatory agreements before disbursing funds to its recipients of the Residential Development Loan Program.

HCD's Action: Corrective action taken.

HCD explained that CalHome Program's ability to grant an 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. Therefore, it developed and implemented a procedure for granting advances in excess of 25 percent to recipients of its CalHome Program 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. HCD believes that this procedure ensures that the appropriate controls are in place. Further, HCD asserted that the two instances of noncompliance identified by the bureau were traced back to two staff members who no longer work for HCD. To ensure that subsequent infractions of the procedure do not occur, HCD indicated it has reissued the procedure to all CalHome Program staff members.

Further, according to HCD, status reports from recipients of its CalHome Program are due 30 days after the end of every quarter. It indicated that as contractors receive an award, they are added to a quarterly report tracking log. According to HCD, staff previously kept their own log; however, that log will now be centralized. If reports are late, HCD stated that its staff will call or email the contractor and note on the log who called, who the contact was, the date called, and the result. It also indicated that the log will be reviewed periodically by the manager and follow-ups will be performed as necessary.

Finance Agency's Action: Partial corrective action taken.

Finance Agency agrees this is an important safeguard that should be implemented. According to the Finance Agency, it has already contacted all awardees requesting this documentation and amended its monitoring procedures to include requiring a copy of the recorded regulatory agreement prior to any future funding disbursements. The Finance Agency added that the majority of the files are now complete, and it expects full compliance from the remaining participants shortly. It also indicated that it suspended any further funding disbursement to localities that have not submitted a copy of a recorded regulatory agreement until they comply with this requirement.

Finding #2: HCD needs to improve its efforts to monitor during the completion phase.

We reviewed the completion phase monitoring for three programs: the CalHome Program, the Emergency Housing and Assistance Program (Emergency Housing Program), and the Multifamily Housing Program-Supportive Housing Program (Supportive Housing Program). 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, 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 three programs. 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 or ensure that sponsors provided appropriate responses. As a result, HCD cannot ensure that sponsors take timely and appropriate corrective action.

We recommended that when practical, HCD should 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. In addition, HCD should ensure it promptly communicates 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.

HCD's Action: Partial corrective action taken.

HCD stated that it 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 Program. It indicated that it has also re-examined and re-communicated its travel expenditure policy to support field visits to conduct site monitoring.

In addition, HCD concurs that it is important to communicate concerns and findings identified during on-site visits to the contractors. HCD explained that there has been a longstanding documented process for such communication, which includes that such letters are required to be prepared by CalHome Program staff within a defined time frame. However, according to HCD, during a change in management, it inadvertently did not approve or did not send these letters to the contractors. HCD stated that 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. It also asserted that the original documentation will be stored in the contractor's file. Finally, HCD indicated that 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.

Finding #3: HCD has not yet completed its verification of data transferred to a new system.

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.

We recommended that HCD complete its review of the accuracy of the data transferred to CAPES and ensure that its clean-up efforts are thoroughly documented and retained for future reference.

HCD's Action: Pending.

HCD concurs with the necessity to complete its review of the accuracy of the data transferred to CAPES. Due to time and staffing constraints, it indicated that it was not possible to check all data prior to the conversion process, as would have been ideal. Subsequently, HCD stated it developed a comprehensive clean-up 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, it also indicated that the continuing staffing limitations as a result of the State's fiscal situation has impeded HCD's efforts to complete the entire clean-up process prior to this audit by the bureau. Finally, HCD plans to finish the clean up of the CAPES data by March 2010, and ensure that thorough documentation of the clean-up efforts will be available at the next periodic visit by the bureau.

Finding #4: Certain programs funded by Proposition 1C are not subject to periodic audits by the bureau.

The Housing and Emergency Shelter Trust Fund Act of 2006 (Proposition 1C) currently does not require the 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.

We recommended that 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.

Legislative Action: Unknown.

We are not aware of any legislative action at this time.