

## **Management Response To The OIG Report On Management And Performance Challenges**

The Department's management and the OIG have worked in a close, collaborative manner during the past year, recognizing the challenges facing the Department and the country. Management's comments and updates on the department's progress in addressing each challenge are set forth below.

### **Human Capital Management**

#### *Office of the Chief Human Capital Officer*

HUD agrees with the OIG's assessment of a critical need for the Department to correct shortcomings in Human Capital Management at HUD. The Department followed recommendations from the National Academy of Public Administration (NAPA), the Office of Personnel Management's (OPM), and the U.S. Government Accountability Office (GAO) in framing a set of actions designed to transform human capital programs at HUD. Since a number of these actions did not appear in OIG's report, several of the more important actions, are listed here as supplemental information.

HUD intends to make fact-based workforce decisions using data collected through the Department's Time Estimate and Allocation Mechanism (TEAM). HUD developed the FY 2015 annual budget at a functional level (reflected in 134 functions) for the twenty-one HUD offices using the new functionally organized TEAM data collection system. The Department also used FY 2013 TEAM time and workload data as the baseline to project FY 2015 FTE and funding requirements for the OMB budget submission. A training package for TEAM reporting and data analysis has been developed to train staff to utilize TEAM data to make resource allocation decisions during the annual budget planning process and throughout the year. Over 400 managers, Budget Officers and Analysts, TEAM Program Coordinators, and TEAM National Program Coordinators will participate.

A process to implement the Human Resources End-to-End (HR E2E) solution was initiated in FY 2012 and is still on-going to respond to GAO's recommendation for more definitive strategic management of human capital resources. Implementation of HR E2E will permit the full integration of HUD human resources data for reporting and management purposes. HR E2E includes a talent management component with the capability for effective succession management planning, ongoing workforce analyses, and the creation of a hierarchical organizational view to meet forecasted needs. HR E2E solution is expected to be fully operational in FY 2014.

To establish a clear workforce planning strategy, HUD initiated a comprehensive approach to workforce and human capital strategic planning. The Workforce Planning Committee was established in FY 2012, to address resource management strategies in the Department. The Human Capital Strategy Working Group was created in FY 2013, to develop strategies for the 2014 — 2018 HUD Strategic Plan. In FY 2013, OCHCO/Office of Human Capital Services (HCS) collaborated with OCFO to implement a new process to ensure submission of timely and comprehensive hiring plans. Additionally, second review procedures were initiated to ensure correct coding of SF-50s, Notification of Personnel Action forms, to ensure better controls over the accuracy of processing of personnel actions. The OCHCO Accountability Team worked with HCS to establish protocols and procedures for reviewing the hiring process, from beginning to end. The review team established quality control measures to improve job opportunity announcements, the adjudication of veterans, qualifications analysis, specialized experience, and the

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overall technical aspects of hiring. The Department's revised Human Capital Framework (to be implemented in FY 2014) and HUD's Human Capital Strategic Plan will align with OPM's Human Capital Assessment and Accountability Framework.

*Office of Multifamily Housing*

With reference to the transformation initiative introduced in the Office of Multifamily Housing, the OIG noted a challenge for Multifamily Housing to ensure that this new style of functioning will continue to maintain adequate monitoring of properties and access to clients. In fact, the transformation is designed to enhance monitoring and make local engagement more consistent and efficient across our programs and throughout our geographic footprint.

The "Transformation" initiative, introduced in April 2013, proposes to modernize an operating model that was originally developed in the 1970's. By doing so, Multifamily will adapt industry best practices, improve its ability to manage risk, and increase accountability and consistency nationwide.

Under the new operating model, Multifamily will differentiate between three types of asset managers. The Multifamily portfolio of assets has already been segmented by risk and complexity, so we can match assets with the proper level of staff expertise, rather than by geography. Project Managers (PMs) in Asset Management will be able to monitor their assigned properties more closely. Rather than be tasked with the entire breadth of the portfolio, PMs will manage similar properties, creating specialists in each class of assets (troubled or non-troubled).

Today, PM's perform about 30 different types of activities which include about 115 different tasks, nearly all of which can be performed remotely. Only extraordinary events require on-site asset management visits. Additionally, we will continue to rely on third parties for 'feet on the street,' including both HUD employees and contractors, such as HUD's REAC (Real Estate Assessment Center) and PBCAs (performance-based contract administrators). Travel and third party support will ensure monitoring, as well as access to clients.

On the production side, Multifamily is developing an underwriter model that provides for single-source contacts. Lenders will work with one HUD staff person (with assigned back-up) from the initial application through closing. This increases accountability for HUD staff as well as visibility for the lenders. This system has been tested in the Atlanta Hub with great success. In addition to the Asset Management and Production operational changes outlined above, Multifamily is also planning on augmenting its travel budget to enable staff to conduct quarterly affordable housing preservation visits as well as training one Field Policy & Management staff member in each consolidating office to serve as a local Multifamily representative.

**Financial Management Governance of HUD**

HUD agrees with the observations and conclusions in the OIG report concerning Financial Management Governance at HUD, noting that the Office of the CFO has limited resources and authority with which to structure and execute the financial management controls needed for effective financial management governance.

Plans for improving financial management governance include some of the financial management systems changes discussed in the next section of the OIG report as well implementation of the interagency

agreement (signed August 7, 2013) with the Bureau of the Fiscal Service (BFS) to obtain full Federal shared services support.

It should also be noted that HUD has made substantial progress in effectively monitoring the Department's administrative control of funds. During FY 2013, the OCFO performed 46 compliance reviews to ensure that program offices followed their established funds control plans.

### **Financial Management Systems**

#### *Office of the Chief Financial Officer*

HUD management concurs with the OIG report in the need to implement a new core financial system for HUD. Management offers a few clarifications on matters discussed in the report.

The New Core program's scope is not a good comparison to the HUD Integrated Financial Management Improvement Project (HIFMIP). New Core has a five-year phased implementation approach that will modernize HUD's core financials and other systems, but utilizes a production ready application with the Administrative Resource Center (ARC) of the Bureau of the Fiscal Service (BFS).

- Phase One – migrate HUD's core financial, procurement, time and attendance, and travel system functionalities to a shared services provider
- Phase Two – evaluate the replacement of the functionality in HUD's legacy administrative and accounting system services associated with budgeting, accounting, finance, and reporting with a shared service solution
- Phase Three – evaluate the replacement of the core financials of the Federal Housing Administration (FHA) and the Government National Mortgage Association (Ginnie Mae) in the shared services environment

Regarding an October 1, 2014, "go live" date, October 1, 2014, is the current target working date for implementation of Phase One of New Core. After the requirements gathering and business process validation sessions are completed and all identified gaps are analyzed, New Core will finalize the timeline and sequencing for implementation. Impacts of the Federal Government shutdown have also not been fully determined, since all requirements sessions had to endure re-planning efforts.

Implementation challenges seen with data conversion and legacy system interfaces on the previous HIFMIP project have a completely different approach under New Core.

- New Core is not developing individual interfaces for each mixed system as in HIFMIP, but instead is developing a middleware solution that will transform and translate the mixed system data to enable utilization of the standard Oracle application programming interfaces (APIs) and reduce interface complexity and risk.
- New Core is incorporating the two primary legacy contractors into the project team who support and maintain HUDCAPS and PAS – the core processing legacy applications – with their specialized expertise for interfaces, data conversion, PIH Section 8, and data warehousing.

The New Core program has engaged an Independent Verification & Validation (IV&V) partner to review all New Core activities, provide recommendations, and actively participate in performance improvements early on in the project. The IV&V contractor will report to the Deputy Secretary on project progress.

The combination of the factors described above will help mitigate the risks and challenges experienced during HIFMIP.

*Office of Housing – Federal Housing Administration*

FHA leadership concurs with OIG’s characterization that insufficient and unpredictable funding is the most significant constraint to timely completion of new application development and retiring antiquated legacy systems. We remain committed to transforming through business process reengineering and modernizing associated IT systems that support Single Family, Multifamily and Healthcare (insured and non-insured) programs that enable program success and agile risk management.

**Information Security**

HUD agrees with the OIG’s assessment and aims to implement corrective actions.

**Single Family Programs**

*Office of Single Family Housing*

Over the past five years, FHA has executed the most sweeping changes to its programs and practices in the agency’s nearly eighty year history. Through substantial changes to borrower credit and underwriting requirements and significant increases in mortgage insurance premiums, FHA has ensured that loans being endorsed today are both high quality and priced adequately for the risk they present to FHA’s insurance fund. In fact, books of business insured since FY 2010 have been increasingly more profitable each year. In addition, FHA has significantly improved its counterparty risk management efforts through increased capital requirements for FHA-approved lenders, improved and risk-based reviews of lenders and loan files, and the removal of large numbers of non-compliant lenders. Finally, faced with large numbers of defaulted loans as a result of the recession, FHA has made vast changes to its loss mitigation and asset disposition policies and processes to reduce losses to the insurance fund from non-performing loans, and to increase recoveries associated with loans that cannot be made to re-perform. In total, the changes FHA has made in the past five years have improved the value of FHA’s MMI Fund by more than \$30 billion.

The statement that “FHA now has the authority to seek indemnification from its direct endorsement lenders” is not correct. This authority has been proposed in various legislation, but nothing has passed yet. Thus while FHA can request indemnification from all lenders, we still only have authority to demand indemnification from Lender Insurance (LI) lenders.

In May 2012, Single Family and the OIG reached agreement on a methodology to review loans for which FHA paid a claim on the mortgage insurance (pre-foreclosure and conveyance claims) within 24 months from endorsement date. In September 2012, Single Family implemented the processes and procedures necessary to accomplish this review. The OIG conducted a follow-up audit in FY 2013 to evaluate Single Family’s progress and noted that Single Family’s loan selection algorithm failed to identify all loans for which a claim was paid and that claim reviews were not conducted in a timely manner. Single Family re-evaluated its algorithm and concluded that its initial programming inadvertently omitted certain claim loans. Single Family promptly re-programmed its algorithm to address this deficiency in August 2013. Housing remains committed to reviewing all early cohort claim loans. However, with respect to the OIG’s concern regarding file review timing, Housing has had to integrate this increase in workload to its QC process and manage to do so with existing staff resources. Single Family will



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continue to refine its operations and systems to improve the timeliness and effectiveness of its entire Quality Control (QC) workload, including claim file reviews.

In addition, Single Family has taken several actions over the last year to improve the consistency and effectiveness of underwriting quality reviews, e.g. the process for identifying, classifying and requesting remedies for defects has been standardized across the office, the sampling methodology has been revised to focus on loans with defaults in the first two years. In addition, we've enhanced the transparency of our findings to the lender community through individual meetings and our new Lender Insight Newsletter, which highlights trends and issues based on our underwriting reviews so that lenders can begin taking corrective actions to their processes. Beyond the actions already taken, we continue to take steps to enhance our quality assurance program. In July 2013, Single Family issued an Advance Notice of Proposed Rule-Making seeking comments on several potential areas of enhancements to our quality assurance program. As a result we have identified potential improvements to our process for classifying defects that will provide more transparency and clarity to lenders; we are seeking resources to grow the nominal number of loan file reviews undertaken each year to ensure a more statistically relevant review of our endorsements and we are considering adjustments to our performance standards that will more clearly indicate relative performance of loans and the quality with which loans were underwritten. Thus while we concur with the OIG that enhancements to our quality assurance programs would be beneficial, we are proactively taking steps toward that goal while being mindful of the limited resources at our disposal.

#### *Ginnie Mae*

Ginnie Mae agrees with the Inspector General regarding the need to enhance MBS portfolio monitoring. Ginnie Mae has already taken steps by increasing staff who manage issuer relations and issuer performance. Additionally, Ginnie Mae has developed tools to track and monitor counterparty default risk in its Office of Enterprise Risk Management.

The Inspector General's reference to a large issuer default in 2009 due to irregularities uncovered by Ginnie Mae's monitoring group eventually resulted in a joint effort by the HUD IG, Ginnie Mae, and Department of Justice to recover the funds and prosecute those responsible for the irregularities.

There is currently a trend of private capital entering housing finance, sometimes through private equity funds, but such funds are not themselves the Ginnie Mae counterparty. Ginnie Mae counterparties are held to the same standards no matter the source of their capital. The acquirer of the bankrupt "top tier" lender alluded to in the memorandum is not owned by private equity or hedge funds but rather is publicly-held. Ginnie Mae, because of its approval rights, had the opportunity to perform substantial due diligence before the award of the government-insured MSR portfolio in that instance.

Ginnie Mae has made significant investments recently in procedures to identify situations where there is elevated risk of default. The Office of Enterprise Risk ("ERO") has developed a system that centralizes the identification of counterparty exposure and provides a tool to manage exposure by establishing limits. "CorporateWatch" assigns each Issuer a risk grade that is derived either by leveraging ratings published by external rating agencies for publicly rated institutions or using an internally developed proprietary risk-rating model. Issuers that are assigned one of the two higher grades are automatically placed on the Watch List, and managed according to the Watch List protocols.

While Ginnie Mae has increased staff and brought some key functions in-house, contractors remain critical to Ginnie Mae's operations: Pool processing, field reviews, and systems development are among

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those tasks for which outsourcing remains the Government's best option. Ginnie Mae has requested in the FY-2015 budget to increase S&E funds to allow for the transfer of some technical functions from contractors to Ginnie Mae staff. If this funding is approved the risks associated with Ginnie Mae's reliance on contractors will be reduced. Also, Ginnie Mae's Office of the Chief Financial Officer does contract assessment reviews on all contracts that \$1 million is expended on annually. These reviews give Ginnie Mae and the auditor's assurance that the contracts have support for proper invoicing.

**HOME Program**

The Department issued the HOME rule which will mitigate the systemic deficiencies identified in HUD OIG audit reports. The Department has also taken steps to improve HOME program management and will be revising the HOME Monitoring Exhibits in the CPD Monitoring Handbook to add questions that will direct CPD monitors to compare project data entered in IDIS with information in the participating jurisdiction's files.

Also the change in methodology for determining compliance with HOME commitment deadlines is now tied to the elimination of FIFO in CPD programs. CPD has developed a draft plan to eliminate FIFO within IDIS to be completed by June 2016, provided that the Department receives funding to make the necessary changes. CPD has requested roughly \$2.7 million in fiscal year 2014 to begin the project. The latest technical approach will perform the work in three phases.

Phase 1a and 1b will make immediate enforcement to matching of funding amounts to specific grant years. These would be smaller / quicker releases to make quick progress. Phase 2 would address all the various embedded remnants of FIFO throughout the system, and also other issues such as supporting the USSGL at the transaction level. This part would be longer than a 1 year effort.

**Public and Assisted Housing Program Administration**

With reference to remarks made in describing HUD's challenge in monitoring the Housing Choice Voucher program, the OIG mentioned a belief by management of the Office of Public and Indian Housing (PIH) that it will address the limitations cited using the Portfolio Management Tool (PMT) and the Next Generation Management System (NGSM). In this discussion, PIH management has the following points of clarification. While the PMT has recently been implemented, the effectiveness of the NGSM, which is currently under development, is dependent upon the availability of funding to bring the NGSM project to completion. Furthermore, although these tools will assist in the oversight of the program, PIH management notes that HUD will continue to face challenges in monitoring this program unless adequate resources are available to provide data verification via remote and onsite reviews.

In discussing the challenge facing HUD in the monitoring and oversight of PHAs participating in the Moving to Work demonstration program (MTW), the OIG stated a need for HUD to quantify a formal process for terminating participants from the demonstration program for failure to comply with their agreement. With respect to this statement, PIH management points out that MTW agencies are bound both by the terms of standardized MTW agreements and, as all PHAs, by the terms of Annual Contributions Contracts. In the standardized MTW agreements and the Annual Contributions Contracts, the Department has included procedures which have been established to bring agencies back into compliance short of termination, and additionally, to terminate if the agencies fail to follow such measures. In those rare instances in which agencies have failed to meet the terms of either document, the Department has taken appropriate steps and brought such agencies into compliance.

### **Administering Programs Directed Toward Victims of Natural Disasters**

HUD implemented several internal controls to ensure that disaster recovery funds are accurately disbursed in a timely manner. Specifically, HUD placed additional controls on the LOCCS system, including restricting all unbudgeted balances, providing for line-item budgets instead of an undifferentiated grant, and including warning flags for draws over \$5 million and over \$25 million. The flags can only be removed, allowing drawdown completion, after a CPD manager reviews and accepts accompanying documentation. Additionally, HUD's Disaster Recovery Grant Reporting (DRGR) system was integrated with LOCCS on January 5, 2009.

HUD conducts Front-End Risk Assessments (FERAs) for Disaster Recovery grants as those grants are an increase in the established CDBG program funding level. A FERA was conducted for disaster recovery grants awarded to New York for the events of September 11, as well as, the first appropriation for the Gulf Coast recovery states (MS, AL, TX, and LA). HUD acknowledges that the FERAs for subsequent appropriations have not been completed in a timely manner and is revising its internal Disaster Recovery procedures manual to correct this deficiency and can point to measureable improvements this fiscal year. Aside from the appropriation of funds under the Disaster Recovery Appropriations Act, 2013 (P.L. 113-2), FERAs are now in place for all of the Division's disaster recovery appropriations. With respect to the FERA developed to P.L. 113-2, the Division submitted its initial FERA to the Office of the Chief Financial Officer (CFO) within ninety days of the enactment of the appropriation. CFO comments have now been incorporated into the FERA and will be resubmitted to shortly.

Additionally, HUD provides technical assistance to states and HUD CPD Field Office prior to grant awards, including reviewing eligible activities, protocols for waiver requests, etc. CPD also reviews performance data and CDBG audits for each state to identify risks associated with disbursements of formula CDBG funds and compliance with CDBG program requirements. In September 2011, HUD issued the Disaster Recovery Policy and Procedures manual to ensure consistency in program review requires for both headquarters and field staff. Disaster Recovery staff also submitted new risk management guidance for the field as part of the CPD Risk Analysis process that will specifically include a separate analysis of disaster recovery grants. The CDBG-DR risk analysis worksheets have been incorporated into the Grants Management Process (GMP) system for Fiscal Year 12 risk analysis. The Disaster Recovery staff has also submitted an update to the CPD Monitoring Handbook that will include CDBG-DR specific monitoring checklists. A new release for the GMP Monitoring Module was deployed as of September 21, 2012. This release is largely designed to incorporate changes made to existing Exhibits and the addition of new Exhibits as a result of Chg-1 to the *CPD Monitoring Handbook 6509.2 Rev-6*, which was issued in March 2012. As of September 26<sup>th</sup> staff can now directly enter their monitoring information into the GMP Monitoring Module for all Exhibits, including any monitoring that used the new Exhibits, 6-2 through 6-8 (disaster recovery) and/or 8-19 (NSP-3).

Disaster recovery assistance provided by the Federal government is governed by the Stafford Act—which was designed to designate the Federal government as a *supplemental* source of available funding—providing assistance in instances where local, state, private-sector, and nonprofit resources are inadequate in addressing disaster response and recovery. Therefore, the Act forbids a recipient of federal disaster relief benefits from receiving “any part of such loss as to which he has received financial assistance under any other program or from insurance or any other source.” 42 U.S.C. § 5155(a). Further, a recipient of assistance will be liable to the United States “to the extent that such assistance duplicates benefits

*available to the person* for the same purpose from another source.” 42 U.S.C. § 5155(c) (*emphasis added*). FEMA guidance indicates that grants or donations from *private* sources can lead to duplication of benefits under the Stafford Act if the funds are made available to a recipient for the same purpose as a federal program (FEMA Disaster Assistance Policy 9525.3 *Duplication of Benefits – Non-Government Funds*). HUD recently determined that private loans need **not** be included in the DOB analysis. More specifically, a private loan should not reduce the amount of Community Development Block Grant (CDBG) disaster recovery assistance available to an applicant. The Department worked with the Small Business Administration (SBA) to determine the correct usage of CDBG disaster recovery funds in relation to a SBA loan. In addition, the Department has developing guidance on meeting unmet needs and avoiding duplication of benefits with other federal (i.e. FEMA, etc.) programs. The Notice describing how grantees can prevent the duplication of benefits was published in the Federal Register Vol.76, No. 221, dated November 16, 2011.