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State Auditor

A Follow-up Audit Report on

**Hurricane Recovery Funds
Administered by the Department
of Housing and Community
Affairs and the Office of Rural
Community Affairs**

August 2009
Report No. 09-048



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Overall Conclusion

The Department of Housing and Community Affairs and the Office of Rural Community Affairs are responsible for administering a total of \$517,439,236 in funds dedicated to the recovery from Hurricane Katrina and Hurricane Rita. In October 2007, the State Auditor's Office made recommendations regarding each agency's administration of hurricane recovery funds.¹ A summary of each agency's implementation of those recommendations is presented below.

Background Information

While Hurricane Katrina did not make landfall in Texas, the State incurred costs when individuals affected by Hurricane Katrina were evacuated to Texas. Hurricane Katrina made landfall in Louisiana on August 29, 2005. Hurricane Rita made landfall in Texas on September 24, 2005.

Department of Housing and Community Affairs

The Department of Housing and Community Affairs (Department) has fully or substantially implemented 12 recommendations² the State Auditor's Office made in October 2007; however, as of June 5, 2009, the Department had spent \$135,012,143 (31 percent) of the \$440,364,797 in hurricane recovery funds made available to it. Specifically, the councils of governments with which the Department has contracted, as well as the Department's primary contractor, report that:

- As of June 5, 2009, a total of 558 applicants for Round 1 of federal Community Development Block Grant Program funds had been approved to receive assistance. Of those 558 approved applicants, 479 (86 percent) had completed homes and 10 (2 percent) had homes with construction in progress. The councils of governments had received 4,701 applications for Round 1. In addition to the 558 applications approved, 93 applicants withdrew their applications, 257 applicants were not eligible for the program, 13 were in processing, and 3,780 were transferred to the Department's primary contractor for processing under Round 2. Round 1 funds totaling \$42,378,185 became available in May 2006.
- As of June 5, 2009, 1,449 applicants for Round 2 of federal Community Development Block Grant Program funds had been approved to receive

¹ See *An Audit Report on Hurricane Recovery Funds Administered by the Department of Housing and Community Affairs and the Office of Rural Community Affairs*, State Auditor's Office Report No. 08-005, October 2007.

² The prior audit report included a total of 14 recommendations for the Department; however, during this follow-up audit, auditors determined that 2 of those recommendations were no longer applicable (see Chapter 1-D for additional information).

assistance. Of those 1,449 approved applicants, 48 (3 percent) had completed homes and 412 (28 percent) had homes with construction in progress. The Department's primary contractor received 6,383 applications for Round 2, which included 3,780 applications transferred from the councils of governments. In addition to the 1,449 applications approved, 1,479 applicants withdrew their applications, 278 applicants were not eligible for the program, 2,853 were pending processing, 255 were on hold with the contractor, and 21 applicants were on a waiting list. Round 2 funds totaling \$384,571,849 became available in April 2007 and August 2007.

Auditors reviewed housing application data provided by the Department's primary contractor for administration of the Round 2 Community Development Block Grant Program funds. The applications were dated between April 2005 and April 2009. Based on analysis of this data, it takes the Department's primary contractor an average of 4 months to determine applicant eligibility, 3 months to process an application for an eligible homeowner, and 2.5 months to complete a home.

The Department asserts that delays in obtaining proof of property ownership from applicants, obtaining environmental clearances, and checking for duplication of benefits have affected the rate at which hurricane recovery funds have been spent. The Department has begun to monitor funds, but it should continue to work toward addressing delays that have affected the rate at which Community Development Block Grant Program hurricane recovery funds have been spent. It will be important for the Department to address these delays because the Department will be responsible for a portion of the \$1,314,990,193 in federal funds the State has received for recovery costs arising from Hurricane Ike.

Auditors also identified other less significant issues that were communicated separately in writing to the Department.

Table 1 summarizes the award and expenditure of the Department's hurricane recovery funds.

Table 1

Status of the Award and Expenditure of Department of Housing and Community Affairs Hurricane Recovery Funds (as of June 5, 2009)					
Program Used to Administer Funds	Total Funds Available ^a	Date Funds Became Available	Total Funds Awarded	Amount Spent ^b	Percent Spent (of Total Funds Available)
Community Development Block Grant Program (Round 1)	\$42,378,185	May 22, 2006	\$40,109,276	\$30,402,762	72%
Community Development Block Grant Program (Round 2)	321,571,849 63,000,000	April 13, 2007 August 29, 2007	378,733,433	\$94,868,557	25%
HOME Investment Partnership Program	8,986,690 4,145,673	April 17, 2006 December 1, 2006	13,132,363	9,458,423	72%
Bootstrap Program	270,400 12,000	March 1, 2006 June 1, 2006	282,400	282,400	100%
Totals	\$440,364,797		\$432,257,472	\$135,012,143	31%
^a Total funds available includes administrative funds. ^b Amount spent includes administrative expenditures.					

Office of Rural Community Affairs

The Office of Rural Community Affairs (Office) has fully implemented 4 (80 percent) of 5 recommendations the State Auditor's Office made in October 2007. The Office received a total of \$77,074,439 in hurricane recovery funds. Of that amount, the Office awarded \$73,367,198 (95 percent) to local organizations and allocated the remaining \$3,707,241 (5 percent) to administration. As of June 5, 2009, \$44,691,557 (58 percent) of the hurricane recovery funds had been spent. These funds are for projects such as infrastructure repair, debris removal, drainage systems, and repairs to water facilities.

The Office asserts that external factors, such as environmental permit requirements and cost certification requirements, affect the ability of several contracted organizations to spend the funds for Community Development Block Grant Program Round 2. It will be important for the Office to address these delays because the Office will be responsible for a portion of the \$1,314,990,193 in federal funds the State has received for recovery costs arising from Hurricane Ike.

Table 2 summarizes the award and expenditure of the Office's hurricane recovery funds.

Table 2

Status of the Award and Expenditure of Office of Rural and Community Affairs Hurricane Recovery Funds (as of June 5, 2009)					
Program Used to Administer Funds	Total Funds Available ^a	Date Funds Became Available	Total Funds Awarded	Amount Spent ^b	Percent Spent (of Total Funds Available)
Community Development Block Grant Program (Round 1)	\$ 32,144,815	May 22, 2006	\$30,537,574	\$ 30,287,461	94%
Community Development Block Grant Program (Round 2)	44,100,000	April 13, 2007	42,000,000	13,574,472	31%
Shelter Improvement Program	419,524	September 2005 to January 2006	419,524	419,524	100%
Rural Health Program	410,100	October 28, 2005	410,100	410,100	100%
Totals	\$77,074,439		\$73,367,198	\$44,691,557	58%
^a Total funds available includes administrative funds. ^b Amount spent includes administrative expenditures.					

Summary of Management's Response

The Department agreed with the recommendations in this report. Its responses to specific recommendations are presented following the recommendations in the Detailed Results section of this report, and its full responses are presented in Appendix 4.

The Office agreed with the recommendations in this report. Its responses to specific recommendations are presented following the recommendations in the Detailed Results section of this report, and its full responses are presented in Appendix 5.

Summary of Information Technology Review

Auditors reviewed selected Department and Office automated systems that were related to the audit objectives and identified no issues in the reliability and completeness of data used during this audit. Auditors also reviewed information technology controls over three information systems at the Department's primary contractor for Community Development Block Grant Program Round 2 funds.

Although the contractor had information technology controls in place, auditors identified certain weaknesses within those controls that should be addressed (see Chapter 1-E for additional details).

Summary of Objectives, Scope, and Methodology

The audit objectives were to determine (1) the extent to which the Department and the Office have implemented recommendations in *An Audit Report on Hurricane Recovery Funds Administered by the Department of Housing and Community Affairs and the Office of Rural Community Affairs* (State Auditor's Office Report No. 08-005, October 2007) and (2) the amount of hurricane recovery funds the Department and the Office have spent.

The audit scope included following up on prior audit recommendations and covered all matters related to the administration of the two awards of Community Development Block Grant Program funds for hurricane recovery, as well as funds from other sources administered after September 1, 2005. The audit scope also included the automated systems and processes that support the functions being audited for the Round 2 of Community Development Block Grant Program funds. Audit work related to automated systems unchanged from the prior audit was limited to determining the reliability of the information in the automated systems.

The audit methodology included collecting information; conducting interviews with staff at the Department, the Office, councils of governments, selected contract administrators, and selected contract recipients; performing selected tests and procedures; and analyzing and evaluating the results of the tests.

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Detailed Results

Chapter 1

The Department Should Continue to Work Toward Addressing Delays That Have Affected the Rate at Which Funds Are Spent and Strengthen Information Technology Controls

The Department of Housing and Community Affairs (Department) has fully or substantially implemented 12 recommendations³ the State Auditor's Office made in October 2007; however, as of June 5, 2009, the Department had spent \$135,012,143 (31 percent) of the \$440,364,797 in hurricane recovery funds made available to it for its three programs.

Chapter 1-A of this report provides information on the Department's expenditures of the primary source of hurricane recovery funds—federal Community Development Block Grant Program funds—and the assistance provided with those funds. Chapters 1-B through 1-D of this report provide information on the status of the Department's implementation of prior audit recommendations for the Community Development Block Grant Program, the HOME Program, and the Bootstrap Program, respectively. Appendix 2 of this report provides information on the time line and availability of funds for the Department's hurricane recovery funds.

The Department also should ensure that its contractor strengthens information technology controls related to the administration of hurricane recovery funds. See Chapter 1-E of this report for additional details.

Chapter 1-A

The Department Should Continue to Work Toward Addressing Delays That Have Affected the Rate at Which Community Development Block Grant Program Funds Are Spent

The Department's subrecipients and contractors had spent 29 percent of the Community Development Block Grant Program Funds as of June 5, 2009.

As of June 5, 2009, the councils of governments and the Department's contractors had spent \$122,404,072 (29 percent) of the \$418,842,709 in Community Development Block Grant Program funds available to them. The Department contracted with three councils of government to administer the housing funds for the Community Development Block Grant Program Round 1. It contracted with several rental housing contractors, the City of Houston,

³ In *An Audit Report on Hurricane Recovery Funds Administered by the Department of Housing and Community Affairs and the Office of Rural Community Affairs* (State Auditor's Office Report No. 08-005, October 2007), the State Auditor's Office made a total of 14 recommendations. However, during this follow-up audit, auditors determined that 2 of those recommendations were no longer applicable (see Chapter 1-D for additional information).

and Harris County for the administration of the housing funds for the Community Development Block Grant Program Round 2.

Community Development Block Grant Program, Round 1. The U.S. Department of Housing and Urban Development (HUD) awarded Texas \$74,523,000 on May 22, 2006; of that amount, \$42,378,185 was designated for housing activities and administrative expenditures. As of June 5, 2009 (approximately 3 years after HUD awarded the funds), the councils of governments with which the Department contracted had spent \$29,250,470 (73 percent) of the \$40,109,276 made available to them.

As of June 5, 2009, the councils of governments reported that a total of 558 applicants for Community Development Block Grant Program Round 1 funds had been approved to receive assistance. Of those 558 approved applicants, 479 (86 percent) had completed homes and 10 (2 percent) had homes with construction in progress.

The councils of governments received 4,701 applications for Round 1 funds. In addition to the 558 applications approved, 93 applicants withdrew their applications, 257 applicants were not eligible for the program, 13 were in processing, and 3,780 were transferred to the Department's primary contractor for processing under Round 2.

Community Development Block Grant Program, Round 2. HUD awarded Texas \$365,571,849 on April 13, 2007, and \$63,000,000 on August 29, 2009; of those amounts, the Department designated \$384,571,849 for housing, evacuee services, and administrative expenditures. As of June 5, 2009 (approximately 2 years after HUD awarded the funds), the Department's contractors had spent \$30,111,877 (13 percent) for the Homeowner Assistance Program and Sabine Pass Restoration Program, and \$32,140,685 (39 percent) for the Rental Housing Stock Restoration Program. As of June 5, 2009 (approximately 1.5 years after HUD awarded the funds), the City of Houston had spent \$27,476,623 (65 percent), and Harris County had spent \$3,424,417 (16 percent) for evacuee services, housing activities, and public safety programs.

As of June 5, 2009, the Department's primary contractor reported that 1,449 applicants for Community Development Block Grant Program Round 2 funds had been approved to receive assistance. Of those 1,449 approved applicants, 48 (3 percent) had completed homes and 412 (28 percent) had homes with construction in progress.

The Department's primary contractor received 6,383 applications for Round 2 funds, which included 3,780 applications transferred from the councils of governments. In addition to the 1,449 applications approved, 1,479 applicants withdrew their applications, 278 applicants were not eligible for the program, 2,853 were pending processing, 255 were on hold with the contractor, and 21 applicants were on a waiting list.

The Department's primary contractor for Round 2 funds takes an average of 4 months to determine applicant eligibility, 3 months to process an application for an eligible homeowner, and 2.5 months to complete a home.

Auditors reviewed housing application data provided by the Department's primary contractor for administration of the Community Development Block Grant Program Round 2 funds. The applications were dated between April 2005 and April 2009. Based on analysis of this data:

- It takes the primary contractor an average of 4 months to determine applicant eligibility. This process begins when the contractor receives the application packet and is awaiting additional documentation from the applicant to complete the application. This process ends when the contractor deems the applicant to be eligible. It should be noted that it takes the contractor an average of 2.4 months to determine applicant eligibility after the applicant has provided all required documentation.
- It takes the primary contractor an average of 3 months to process an application for an eligible homeowner through the grant determination stage. This process begins with the initial inspection of the home and ends with the contractor reviewing the application to determine the amount and type of assistance. This stage includes the contractor performing duplication of benefits determination, the contractor obtaining bids from building contractors, the applicant selecting the home plan, and the contractor conducting the site-specific environmental review.
- It takes the primary contractor an average of 2.5 months to complete construction of a home. This process begins with the contractor preparing the closing documents for the applicant to approve and ends when the home construction is completed. It should be noted that auditors calculated this average using the construction complete date in the application data, and this date does not correspond to a document date (such as a final inspection). Instead, the construction complete date can automatically be changed by the contractor's system when other changes are made to the applicant's file (see Chapter 1-E for additional information).

The Department asserts that delays in obtaining proof of property ownership from applicants, obtaining environmental clearances, and checking for duplication of benefits have affected the rate at which Community Development Block Grant Program hurricane recovery funds have been spent. Specifically:

- **Proof of property ownership.** Although the Department asserts that there are delays in obtaining proof of ownership, it does not retain documentation showing how long it takes to obtain this information from applicants. However, it is important to note that both an April 2009 Department

governing board decision and House Bill 2450 (81st Legislature, Regular Session) now enable the Department to obtain an affidavit from the applicant asserting that the applicant is the property owner for certain types of assistance programs.

- Obtaining environmental clearances. HUD regulations require two types of environmental clearances before it will release funds. The first, broad-level review clearances, took between 2 and 3 months to obtain for Round 1 funds and between 12 and 17 months to obtain for Round 2 funds. The second, site-specific environmental clearances, take an average of 14 to 45 calendar days to obtain, according to Department information. The broad-level review clearances for Round 1 involved less complicated requirements due to the lower dollar amount of the Round 1 funds and the number of homes receiving assistance. The broad-level review clearance for Round 2 involved an environmental assessment that considers such factors as land development, noise, air quality, historical values, urban impact, socioeconomic factors, and community facilities and services. That environmental assessment was required due to the large amount of Round 2 funds and the number and proximity of homes receiving assistance.
- Checking for duplication of benefits with Hurricane Ike funds. The councils of governments and the Department's primary contractor must verify that each applicant is not receiving assistance from multiple sources for the same damage. The Department worked with HUD to obtain clarification of its procedures regarding applicants affected by both Hurricane Rita and Hurricane Ike. In November 2008 the Department submitted questions to HUD regarding how to avoid duplication of benefits for applicants whose homes received damages from both Hurricane Rita and Hurricane Ike. The Department received the answers to its questions in March 2009.

The Department has begun to implement monitoring efforts.

The Department has begun to monitor the Community Development Block Grant Program funds, but it should continue to work toward addressing delays that have affected the rate at which those funds have been spent. To initiate monitoring efforts, the Department:

- Conducted contract monitoring reviews of the councils of governments between fiscal years 2005 and 2009 for Round 1 funds. The Department performed contract monitoring risk assessments of the contracts for Round 2 funds in January 2009, and conducted its initial on-site contract monitoring review visits between October 2008 and May 2009.
- Conducted on-site fiscal monitoring visits at its primary contractor for Round 2 funds in June 2008 and February 2009. During these monitoring visits, the Department reviewed expenditures to ensure they were

allowable. During its June 2008 monitoring visit, the Department noted instances in which the contractor did not have supporting documentation for certain expenditures. The contract between the Department and the primary contractor was effective on December 31, 2007.

- Conducted an on-site program monitoring visit at its primary contractor for Round 2 funds in May 2009. In that visit, the Department reviewed the application process to ensure that applicants were eligible and benefits were calculated correctly, and it performed testing of the contractor's environmental reviews to ensure they were completed in accordance with regulations. The Department estimated that it would release its report from that review in July 2009.
- Conducted on-site fiscal monitoring visits from May 2008 through December 2008 at the City of Houston and Harris County, both of which received funds directly from the Department to assist individuals affected by Hurricane Katrina who were evacuated to Texas. During these visits, the Department reviewed expenditures to ensure they were allowable. From these reviews, the Department concluded that it observed sufficient evidence to support a conclusion that the City of Houston and Harris County were in compliance with federal and state requirements. The contracts between the Department and the City of Houston and Harris County were effective on August 29, 2007.
- Is in the process of developing procedures to monitor \$42 million in funds that were set aside for special needs applicants. These funds are part of the Round 2 Homeowner Assistance Program and are targeted specifically for persons with special needs, including persons with disabilities, the elderly, persons with alcohol or drug additions, persons with HIV/AIDS, and public housing residents.
- Has begun to review whether its primary contractor for Round 2 funds has met the "service levels" in its contract with the Department. If the contractor does not provide services in accordance with the service levels set forth in the contract, the contractor is required to apply credits against the fees it charges the Department. The Department has performed a preliminary analysis of the contractor's service levels and calculated \$59,760 in credits, but it has not required the contractor to deduct those credits from the fees the contractor charges. The Department is performing an additional analysis to determine whether the service levels in the contract should be amended or whether new service levels should be added. The contract between the Department and the primary contractor was effective on December 31, 2007.

It will be important for the Department to ensure that it continues to work toward addressing delays that have affected the rate at which Community Development Block Grant Program hurricane recovery funds have been spent

because the Department will be responsible for a portion of the \$1,314,990,193 in federal Community Development Block Grant Program funds the State has received for recovery costs arising from Hurricane Ike (see Appendix 3 for additional details).

Recommendation

The Department should continue to work toward addressing delays that have affected the rate at which Community Development Block Grant hurricane recovery funds have been spent.

Management's Response

Management agrees with the recommendation. However, the streamlining suggested by the SAO must be a coordinated effort among a number of federal, state, and local governmental entities, and significant streamlining may not be possible without changes to federal and state laws governing the Community Development Block Grant program.

Disaster response is an urgent need, and where processes can be streamlined or accelerated to bring needed relief more quickly, such improvements will be made. However, they must always be made in a manner that minimizes the risk of fraud, waste, and abuse and provides assurance that these public funds are, in fact, used only to build safe, decent homes for qualified individuals.

During the 81st legislative session, the Legislature provided additional guidance to the Department in order to expedite disaster relief even where recipients could not document legal title to their homes. The Department's Governing Board consequently adopted a policy to move forward with providing relief to these individuals. The Department has worked proactively with ACS, the COGs, and other parties to streamline these processes wherever possible and will continue to seek opportunities to address any delays.

Person Responsible: Kelly Crawford

Target Date for Implementation: September 1, 2009

The Department Fully or Substantially Implemented All Six Prior Audit Recommendations Related to the Community Development Block Grant Program

Implementation Status Definitions

Fully Implemented - Successful development and use of a process, system, or policy to implement a prior recommendation.

Substantially Implemented - Successful development but inconsistent use of a process, system, or policy to implement a prior recommendation.

Incomplete/Ongoing - Ongoing development of a process, system, or policy to address a prior recommendation.

Not Implemented - Lack of a formal process, system, or policy to address a prior recommendation.

The Department fully or substantially implemented all six prior audit recommendations related to the Community Development Block Grant Program in *An Audit Report on Hurricane Recovery Funds Administered by the Department of Housing and Community Affairs and the Office of Rural Community Affairs* (State Auditor’s Office Report No. 08-005, October 2007).

Table 3 provides information on the implementation status of the prior audit recommendations.

Table 3

Status of Implementation of Prior Audit Recommendations Related to the Community Development Block Grant Program	
Recommendation	Auditor Comments
Fully Implemented Recommendations	
1 The Department should ensure that councils of governments have adequate staffing resources dedicated to administering the Community Development Block Grant hurricane recovery funds.	The Department addressed this recommendation by evaluating productivity and providing assistance in the form of stewardship activity to address deficiencies in productivity. The Department supplemented staffing deficiencies at one of the councils of governments by dispatching its own staff to assist with application eligibility processing.
2 The Department should provide councils of governments with consistent written guidance related to maintaining adequate documentation used to make income eligibility determinations for Community Development Block Grant hurricane recovery funds (examples of documentation include pay stub information, tax returns, and documents related to property eligibility and environmental clearances). The Department also should ensure that councils of governments adhere to the prescribed state and federal guidance in awarding Community Development Block Grant funds.	The Department provided its <i>Housing Implementation Manual</i> to the councils of governments at the beginning of Round 1 of the Community Development Block Grant Program, but the original manual did not contain guidelines on specific documents required. However, the current manual includes detailed instructions and forms to use. The Department met with the councils of governments regularly at the beginning of the program and currently provides technical assistance on an as-needed basis.
3 The Department should ensure that councils of governments apply consistent and approved methods to calculate the annualized income of applicants for Community Development Block Grant hurricane recovery funds.	The Department provides guidance on calculating annualized income to the councils of governments through the <i>Housing Implementation Manual</i> . Auditors tested 90 application files at the councils of governments and determined that income calculations were performed in accordance with the manual for all 90 applications.
4 The Department should develop and implement monitoring policies to ensure that councils of governments comply with Community Development Block Grant requirements and contractual obligations. These policies also should detail a process to determine whether applicants have received assistance from multiple agencies for the same damage claims.	The Department has developed and implemented monitoring procedures to ensure that councils of governments comply with Community Development Block Grant requirements and contractual obligations. The Department also has implemented benchmarks for the councils of governments to follow to certify applicants. In addition, the Department certifies the councils of governments’ draw requests.

Status of Implementation of Prior Audit Recommendations Related to the Community Development Block Grant Program	
Recommendation	Auditor Comments
Substantially Implemented Recommendations	
5 The Department should continue to coordinate with councils of governments to identify and eliminate bottlenecks in the eligibility determination process for Community Development Block Grant hurricane recovery funds.	<p>Eliminating the bottlenecks is an on-going process that should continue until the grants and contracts are completed.</p> <p>To address this recommendation, the Department:</p> <ul style="list-style-type: none"> ▪ Obtained guidance from the Texas Historical Commission on what types of projects require historical clearances. ▪ Provided assistance to one of the councils of governments to expedite the eligibility process. ▪ Provided funding from the Housing Trust Fund to homeowners to supplement gaps in assistance and cover the costs of repairing or reconstructing the homes. <p>The Department asserts that obtaining proof of ownership from applicants has affected the rate at which hurricane recovery funds have been spent. The councils of governments are able to accept forms of home ownership other than title documents. The Department did not implement a policy change to accept affidavits regarding ownership until April 2009.</p> <p>See Chapter 1-A for additional information.</p>
6 The Department should implement all recommendations related to councils of governments' oversight listed above when it monitors the program management firm with which it intends to contract to administer the \$222,371,273 from the second round of Community Development Block Grant funding.	<p>To address this recommendation, the Department:</p> <ul style="list-style-type: none"> ▪ Included personnel requirements in its contract with its primary contractor for the Homeowner Assistance Program and the Sabine Pass Restoration Program. ▪ Ensured that the primary contractor's policy and procedures manual includes instructions, required documents, and verification procedures regarding income eligibility determinations for Community Development Block Grant Program hurricane recovery funds. The Department approved the contractor's manual. ▪ Ensured that the primary contractor's policy and procedures manual includes instructions to calculate annualized income to ensure the applicants meet income requirements. Auditors tested 43 application files and determined that income calculations were performed in accordance with the manual for all 43 applications. ▪ Developed and is in the process of implementing monitoring procedures to ensure that the primary contractor complies with Community Development Block Grant Program requirements and contractual obligations. The Department also is evaluating the primary contractor's service levels against contract requirements to determine whether contract amendments need to be made to the existing service levels. In addition, the Department performed a program review at the primary contractor in May 2009 and will begin tracking the \$42,000,000 set-aside for special needs applicants. <p>The Department and its primary contractor assert that obtaining proof of ownership from applicants has affected the rate at which hurricane recovery funds have been spent. However, the Department did not implement a policy change to allow the primary contractor to accept affidavits regarding ownership until April 2009. The contract between the Department and the primary contractor was effective on December 31, 2007.</p> <p>See Chapter 1-A for additional information.</p>

The Department Fully or Substantially Implemented All Five Prior Audit Recommendations Related to the HOME Program

Implementation Status Definitions

Fully Implemented - Successful development and use of a process, system, or policy to implement a prior recommendation.

Substantially Implemented - Successful development but inconsistent use of a process, system, or policy to implement a prior recommendation.

Incomplete/Ongoing - Ongoing development of a process, system, or policy to address a prior recommendation.

Not Implemented - Lack of a formal process, system, or policy to address a prior recommendation.

The Department fully or substantially implemented all five prior audit recommendations related to the HOME Program in *An Audit Report on Hurricane Recovery Funds Administered by the Department of Housing and Community Affairs and the Office of Rural Community Affairs* (State Auditor's Office Report No. 08-005, October 2007).

Table 4 provides information on the implementation status of the prior audit recommendations.

Table 4

Status of Implementation of Prior Audit Recommendations Related to the HOME Program	
Recommendation	Auditor Comments
Fully Implemented Recommendations	
1 The Department should implement its plans to align all significant responsibilities pertaining to the HOME Program within the chain of command of the HOME Program director.	The Department's HOME Division formed and staffed its performance group in October 2007. As of March 1, 2009, the Department shifted responsibilities within the HOME Division to designate a single point of contact for the HOME contract administrators.
2 The Department should ensure that it secures environmental clearances before incurring reconstruction or replacement costs for projects funded with HOME Program funds.	The Department's HOME Division's procedures specify that environmental clearances are to be obtained prior to a project being set up. Auditors performed data analysis for all HOME disaster contracts and confirmed that the contract set-up dates were after the environmental clearance dates. Auditors also tested 30 HOME disaster contract draws and determined that all 30 were paid after the environmental clearances had been obtained.
3 The Department should ensure that its staff validates all costs on invoices that contractors submit for projects funded with HOME Program funds, and compare those costs with amounts allowed under the contract.	The Department's contract management system includes edit checks to prevent draw requests from being processed for amounts that exceed contract budget amounts. Auditors tested 30 HOME disaster contract draws and determined that all 30 were allowable draws for which the Department had validated costs.
4 The Department should ensure that all property owners are listed on applications for HOME Program funds (and particularly on the demolition approval form within the application).	Auditors tested 30 HOME disaster contract files and determined that all 30 included the applicants' signatures on all required contract documentation.

Status of Implementation of Prior Audit Recommendations Related to the HOME Program	
Recommendation	Auditor Comments
Substantially Implemented Recommendation	
5 The Department should continue efforts to accelerate the expenditure of HOME Program funds for hurricane recovery.	The Department's HOME Division provides contract administrators with the <i>HOME Owner Occupied Assistance Manual</i> , which provides guidance on home ownership documents; it also provides guidance on home ownership requirements to administrators on an individual basis. However, the HOME Division does not track how long it takes to obtain proof of home ownership. The Department's Legal Services Division prepares legal documents from draft documents prepared by HOME Division staff, and it asserts that missing or incorrect information slows the process (see additional details below this table).

The Department and counties' contract administrators asserted that obtaining title documents from applicants and conducting environmental reviews contributed to delays in spending HOME Program disaster recovery funds.

Proof of Ownership. The Department entered into 19 contracts with counties to administer HOME Program disaster recovery funds through grants or loans. The contract administrators for the counties are responsible for obtaining proof of ownership documentation from the applicants, but the Department does not track how long it takes for contract administrators to obtain the documentation.

The Department's HOME Program staff provides guidance related to obtaining ownership documents to the contract administrators through the *HOME Division Owner Occupied Assistance Manual* and on an individual basis. The manual lists the eligible forms of proof of home ownership and the process for verifying ownership and eligibility.

There are more strict documentation requirements for loans provided with HOME disaster recovery funds because, in the case of loans, the Department must put a lien on the property to protect the State's interest. For HOME Program loans, the contract administrator also must obtain a title commitment and ownership documentation to establish clear ownership of the property. For HOME Program grants, an applicant must prove only home ownership and program eligibility.

To prepare the final loan documents, the Department's Legal Services Division reviews the documentation gathered and prepared by the contract administrators and the Department's HOME Program staff. External factors, such as divorce or a death in the applicant's family, can complicate the process of establishing clear ownership of a property. The Department also asserts that missing documentation contributes to delays in establishing clear ownership.

Levels of Environmental Reviews

HUD requires two levels of environmental reviews in order to release funds:

- **Broad-level reviews** involve publishing a notice of intent to request release of funding from HUD and public comment periods. "Tiering" is a term used for a broad review of environmental issues that can be readily addressed and is performed to eliminate repetitive, site-specific review
- **Site-specific reviews** can reference or summarize information obtained through a broad-level review.

Environmental Reviews. The counties' contract administrators submit "Proof of Publishing" and a "Request for Release of Funds" to the Department as part of the broad-level environmental review process (see text box for additional information). The Department forwards this information to the U.S. Department of Housing and Urban Development (HUD). If no significant complaints are filed within a specified comment time period, HUD then releases the funds. Comment periods have two parts: (1) the local public comment period, which ranges from 7 to 15 days (based on the level of environmental review) and is open to any type of comment or concern and (2) the HUD comment period, which is always 15 days and is open to only comments regarding procedural errors related to the requested release of funds. The counties may be

exempt from the "Request for Release of Funds" process and the public comment periods if the activities qualify as exempt under HUD environmental regulations.

Of the 19 contracts between the Department and counties that administer HOME Program disaster recovery funds:

- Seventeen counties performed a broad-level review and obtained approval from HUD to release funds within time frames ranging from 5 and 112 calendar days, and
- Two counties' contracts were canceled and the funds were deobligated because the counties were unable to identify eligible applicants.

Auditors reviewed 30 HOME disaster recovery project files and determined that it took an average of 15 calendar days for the counties to obtain a site-specific environmental review.

Contract administrators for the counties have spent 72 percent of HOME Program disaster recovery funds and have identified 195 homeowners to assist.

The Department awarded \$13,506,763 in HOME Program disaster recovery funds to 19 counties. Two of the counties were unable to identify eligible applicants and the Department subsequently deobligated both contracts, which totaled \$374,400 (3 percent of the total amount awarded to the counties). The total amount awarded for the remaining 17 contracts was \$13,132,363.

As of June 5, 2009 (approximately 3 years after the funding became available), the contract administrators for the counties had spent \$9,458,423 (72 percent) of the \$13,132,363, and the contract administrators had identified 195 homeowners to assist.

The Department Fully Implemented the Applicable Prior Audit Recommendation Related to the Bootstrap Program

Implementation Status Definitions

Fully Implemented - Successful development and use of a process, system, or policy to implement a prior recommendation.

Substantially Implemented - Successful development but inconsistent use of a process, system, or policy to implement a prior recommendation.

Incomplete/Ongoing - Ongoing development of a process, system, or policy to address a prior recommendation.

Not Implemented - Lack of a formal process, system, or policy to address a prior recommendation.

The Department fully implemented one of three prior audit recommendations related to the Bootstrap Program in *An Audit Report on Hurricane Recovery Funds Administered by the Department of Housing and Community Affairs and the Office of Rural Community Affairs* (State Auditor’s Office Report No. 08-005, October 2007). The two remaining audit recommendations were no longer applicable after the Department deobligated the remaining Bootstrap Program funds.

Table 5 provides information on the implementation status of the prior audit recommendations.

Table 5

Status of Implementation of Prior Audit Recommendations Related to the Bootstrap Program	
Recommendation	Auditor Comments
Fully Implemented Recommendation	
1 The Department should deobligate Bootstrap Program funds awarded to organizations that cannot fulfill their responsibilities and reallocate those funds to other organizations that can fulfill program requirements. Alternatively, it should reallocate Bootstrap Program funds to another program capable of delivering hurricane recovery funds to eligible individuals.	The Department deobligated \$1,610,400 in Bootstrap Program disaster recovery funds from the three non-profit organizations with which it had contracted. The Department returned the funds to the Housing Trust Fund (which is not specifically designated for disaster recovery).
Recommendations That Are No Longer Applicable	
2 The Department should identify and eliminate bottlenecks delaying the delivery of hurricane recovery funds through the Bootstrap Program.	The Department initially provided more hands on-training and technical assistance in the form of training sessions to Bootstrap Program disaster recovery recipients. However, this effort was not successful, and the Department ultimately deobligated the Bootstrap Program funds. After the Department deobligated the funds, this audit recommendation was no longer applicable.
3 The Department should ensure that Bootstrap Program participants obtain the required owner-builder education certificates and that the Department maintains this documentation.	After the Department de-obligated the Bootstrap Program disaster recovery funds, this audit recommendation was no longer applicable.

The Department Deobligated Remaining Bootstrap Program Funds

In December 2005, the Department made \$1,892,800 of its Bootstrap Program funds available to organizations assisting individuals or families who were affected by Hurricane Rita. These funds were intended for the purchase or refinance of (1) real property on which to build new residential construction or (2) improvements to existing residential housing through self-help construction for very low- and extremely low-income individuals and/or families (owner-builders), including persons with special needs. Eligible applicants were nonprofit organizations certified by the Department as “Nonprofit Owner-Builder Housing Programs” as defined in Texas Government Code, Section 2306.755.

The Department contracted with three organizations to administer these Bootstrap Program funds. Only one of the organizations assisted any households: It provided loans to 16 households totaling \$260,000. Two of the organizations spent \$22,400 for administrative expenses and the third organization spent no funds. The total amount spent from the Bootstrap Program on disaster recovery was \$282,400. The Department deobligated the remaining \$1,610,400 in January 2008, May 2008, and December 2008 and returned the funds to the Housing Trust Fund (which is not specifically designated for disaster recovery).

The Department Should Ensure That Its Contractor Strengthens Information Technology Controls Related to the Administration of Hurricane Recovery Funds

The Department contracted with a contractor to administer the Homeowner Assistance Program and the Sabine Pass Restoration Program, which will distribute \$232,954,100 (61 percent) of the Round 2 Community Development Block Grant Program funds. Auditors reviewed information technology controls over the three information systems the contractor uses to administer these programs (see the text box for additional details). The controls reviewed included user access and security; data input, output, and processing controls; software interfaces; application code changes; computer room physical security; and disaster recovery.

Contractor Information Systems Tested

The Department's primary contractor and its two sub-contractors use three information systems to administer the Homeowner Assistance Program and the Sabine Pass Restoration Program:

- One system is used to manage the entire process from application intake to construction.
- A second system processes housing request applications to determine applicant eligibility and benefits.
- A third system processes payments to contractors throughout the construction process.

Although the contractor had information technology controls in place for the three information systems tested, auditors identified weaknesses within those controls that should be addressed to ensure compliance with the Texas Administrative Code and the contract between the contractor and the Department. Specifically, auditors identified weaknesses in the following areas:

- **Access controls.** Individuals whose employment with the contractor had been terminated still had active user accounts for the three information systems tested. Contractor employees who were not assigned to the Homeowner Assistance Program or the Sabine Pass Restoration Program also had access to the three information systems tested. In addition, users access these three systems using generic user IDs (rather than unique, user-specific user IDs) that allow changes to information or the viewing of personal information.

Title 1, Texas Administrative Code, Section 202.25, requires that access to information resources be managed to ensure authorized use; that confidential information be accessible only to authorized users; that each user of information resources be assigned a unique identifier; and that a user's access authorization be appropriately modified or removed when the user's employment status or job responsibilities within the state agency change.

Weaknesses in access controls could result in unauthorized access to confidential information and changes to data that could not be traced to a specific user.

- **Passwords.** User passwords lack complexity and do not expire for (1) the system the contractor uses to manage the application and construction

process and (2) the system the contractor uses to process payments to building contractors.

The contractor's contract with the Department specifies that the contractor's password policy must require the following elements: minimum length, combination of alpha and numeric or special characters, and password duration and rotation. The contractor has not enabled the password duration and complexity features in the system it uses to manage the application and construction process. The system the contractor uses to process payments to building contractors was developed by a third party and lacks application-level security.

Passwords that do not expire or lack complexity may increase the risk of unauthorized access to information systems.

- **Change control.** The contractor has not documented the application change control and testing process for the system it uses to manage the application and construction process. Instead, the contractor uses an informal and undocumented change control process.

Title 1, Texas Administrative Code, Section 202.25 (7), states that a state agency head or designated representative and information security officer shall create, distribute, and implement information security policies to include establishing the process for controlling modifications to hardware, software, firmware, and documentation to ensure the information resources are protected against improper modification before, during, and after system implementation.

Without a documented change control process, key components of coding, testing, and quality assurance may not be performed or documented properly. This could result in errors in code that may not be readily detectable and traceable.

- **Off-site storage and back-up.** The contractor's San Antonio location has no off-site storage for backup files. The on-site location in San Antonio houses the servers for the three information systems that auditors tested, and this is the same location at which the contractor stores backup files.

Title 1, Texas Administrative Code, Section 202.25 (7), states that a state agency head or designated representative and information security officer shall create, distribute, and implement information security policies to include establishes the rules for the backup, storage, and recovery of electronic information.

Not storing backup files off site increases the risk of complete loss of data due to fire, wind, water, or other destruction of the facility.

- Data input. Within the system that the contractor uses to manage the application and construction process, the field that tracks the completion date for construction can change automatically when there are other activities for that home. The contractor defines this field as “The [date on which] final inspection has been completed and we are waiting for final approval from the contractor to conclude the process.” However, the construction complete date is not a user-entered field that is tied to a final inspection document date. Instead, the construction complete date is based on a change made by the contractor to the applicant status within the system, and an applicant can move in and out of that status under limited circumstances. When this happens, the construction completion date is automatically updated in the system with the date of the most recent event. Therefore, because the construction completion date can change multiple times in the system for a single home, it can be difficult to determine the actual construction completion date.

Recommendations

The Department should monitor the information systems of the contractor to ensure compliance with the contractual provisions related to information system controls. Specifically, the Department should:

- Ensure that the contractor assigns unique user IDs to each individual who uses its information systems.
- Ensure that the contractor removes or disables user IDs for its information systems for terminated employees or employees who are not assigned to the Homeowner Assistance Program or the Sabine Pass Restoration Program.
- Ensure that the contractor enables user password expiration and password complexity within the system the contractor uses to manage the application and construction process.
- Ensure that the contractor implements controls that compensate for the password weaknesses in the system the contractor uses to process payments to building contractors.
- Ensure that the contractor documents, tests, and communicates the key components of its information system change control process.
- Ensure that the contractor stores backup data off site.

- Work with the contractor to tie the construction completion date in its information system to a static date that corresponds to a document, such as a final inspection report or a certificate of occupancy.

Management's Response

Management agrees with the recommendation and will work with ACS to ensure that their information technology controls are strengthened. TDHCA's Information Technology staff and Disaster Recovery & Emergency Housing staff will meet with ACS and ensure that the necessary measures are taken and that the recommended controls are implemented.

Person Responsible: Curtis Howe

Target Date for Implementation: September 1, 2009

The Office Has Fully Implemented Four of Five Prior Audit Recommendations

Implementation Status Definitions

Fully Implemented - Successful development and use of a process, system, or policy to implement a prior recommendation.

Substantially Implemented - Successful development but inconsistent use of a process, system, or policy to implement a prior recommendation.

Incomplete/Ongoing - Ongoing development of a process, system, or policy to address a prior recommendation.

Not Implemented - Lack of a formal process, system, or policy to address a prior recommendation.

The Office of Rural Community Affairs (Office) has fully implemented four (80 percent) of five recommendations in *An Audit Report on Hurricane Recovery Funds Administered by the Department of Housing and Community Affairs and the Office of Rural Community Affairs* (State Auditor’s Office Report No. 08-005, October 2007).

The Office is working with its grants management system provider to implement the prior audit recommendation to reconcile the information in its accounting system to its grants management system.

Table 6 provides information on the implementation status of the prior audit recommendations.

Table 6

Status of Implementation of Prior Audit Recommendations	
Recommendation	Auditor Comments
Fully Implemented Recommendations	
1 The Office should document its verification that Community Development Block Grant sub-recipients are not suspended or debarred before it awards contracts.	The Office has included language in its new Community Development Block Grant Program disaster contracts to certify that subrecipients are not suspended or debarred. (This language was not present in the contracts for Round 1 of Community Development Block Grant Program funds.) When the applicants apply for the funding, they are now required to sign the contract and self-certify that they are not suspended or debarred from contracting and receiving funds. Auditors tested the eight contracts for Round 2 of Community Development Block Grant Program funds and determined that all eight contained the certification language and were signed by the subrecipient.
2 The Office should develop and implement a process to consistently verify that Community Development Block Grant sub-recipients provide evidence of sufficient oversight of their financial processes.	In response to this recommendation, the Office incorporated Policy CDBG 08-01 into its <i>Implementation Manual</i> to provide its Community Development Block Grant Program contractor localities with guidance on documentation they must submit to demonstrate the financial capacity required to receive and manage grant funds. Auditors tested the eight contracts for Round 2 of Community Development Block Grant Program funds and determined that all eight contract files contained current audit reports.

Status of Implementation of Prior Audit Recommendations	
Recommendation	Auditor Comments
3 The Office should retain documentation it uses to verify recipients' eligibility for Rural Health Disaster Relief and Recovery Grant funds.	The Office's Rural Health Division's operating procedures now specify that certain criteria must be met in order to be eligible for Rural Health Disaster Relief and Recovery Grant Funds. These new procedures were implemented for a new disaster program to address Hurricane Ike starting in October 2008. There have been no new Rural Health Division expenditures for Hurricane Rita since the prior State Auditor's Office audit. The first opportunity to implement the new procedures was solely for Hurricane Ike. Audit testing of the two new Rural Health Disaster Relief and Recovery contracts determined that the Rural Health Division staff retained documentation used to verify recipients' eligibility for Rural Health Disaster Relief and Recovery funds.
4 The Office should reconcile its accounting system with the Uniform Statewide Accounting System (USAS) in a timely manner and ensure that all variances between the two systems are researched, documented, and corrected.	The Office reconciles its accounting system to USAS on a monthly basis in accordance with its Finance Division's policy and adequately documents, researches, and corrects variances identified during this reconciliation.
Ongoing/Incomplete Recommendations	
5 The Office should reconcile information in its accounting system to information in its grants management system on a regular basis.	The Office currently has no procedures to reconcile its accounting system to its current grants management system. However, the Office has signed a contract with a provider to develop a new grants management system. A requirement for a reconciliation feature between the grants management system, the federal reporting system for the Community Development Block Grant Program, the Office's accounting system, and USAS is included in that contract's scope of work.

The Office awarded all of its hurricane recovery funds.

The Office received a total of \$77,074,439 in hurricane recovery funds. Of that amount, the Office awarded \$73,367,198 (95 percent) to local organizations and allocated the remaining \$3,707,241 (5 percent) to administration. As of June 5, 2009, \$44,691,557 (58 percent) of the hurricane recovery funds had been spent for all three programs.

Community Development Block Grant Program. These funds are spent for projects such as infrastructure repair, debris removal, drainage systems, and repair of water facilities. The U.S. Department of Housing and Urban Development (HUD) made available to the Office \$30,537,574 for Round 1 and \$42,000,000 for Round 2 for non-housing disaster recovery activities.

The Office awarded all of its available non-housing funds to 98 local organizations for Round 1 and to 8 local organizations for Round 2. The organizations with which the Office contracted for Round 1 funds had spent \$28,883,402 (95 percent) of these funds as of June 5, 2009 (approximately 3 years after the funds became available). The 8 organizations with which the Office contracted with for Round 2 funds had spent \$13,076,032 (31 percent) of these funds as of June 5, 2009 (approximately 2 years after the funds

became available). The Office asserts that external factors affect the ability of several contracted organizations to spend Round 2 funds. Specifically:

- One organization has completed its public facilities rehabilitation and demolition project work, but it was not able to draw its remaining funds until it obtained a cost certification to clarify reimbursement requests to prevent duplication of benefits payments from multiple HUD funding sources. The Office will be able to request this organization's remaining \$4,115,570 in funds after the Office and HUD receive and approve the cost certification report.
- One organization that contracted with the Office for flood and drainage facility projects experienced delays while undergoing review by the U.S. Corps of Engineers for potential Clean Water Act permitting requirements. The Corps of Engineers approved the debris removal portion of the projects on January 13, 2009, and it approved the drainage facilities portion of the projects on April 14, 2009. This organization has \$4,538,431 in funding remaining for these projects.
- One organization that contracted with the Office for flood and drainage facility projects experienced delays while undergoing review by the U.S. Corps of Engineers and by an engineering contractor for potential Clean Water Act permitting requirements. The Corps of Engineers approved two of this organization's proposed three drainage ditch improvement projects on November 18, 2008. In addition, this organization requested that projects be added to its contract. The Office is reviewing the additional activities to determine whether they qualify under the Community Development Block Grant Program. This organization has \$4,410,505 in funding remaining for these projects.

It will be important for the Office to ensure that it continues to work toward addressing delays that have affected the rate at which Community Development Block Grant Program hurricane recovery funds have been spent because the Office will be responsible for a portion of the \$1,314,990,193 in federal Community Development Block Grant Program funds the State has received for recovery costs arising from Hurricane Ike.

Rural Health Disaster Relief and Recovery Program. These funds are spent for projects such as (1) emergency acquisition, construction, repair, or improvement of facilities or equipment, (2) pharmaceuticals and medical supplies, (3) first aid and life-saving equipment and supplies for first-response situations, and (4) infection control supplies. Applicants for this funding must be in an area with a population of fewer than 150,000 and must be in a medically underserved area or a health professional shortage area.

The Office contracted with 20 organizations and awarded \$420,000 of its capital improvement program funds for this program. Nineteen of the

organizations had spent \$410,100 of the funds awarded as of June 5, 2009. One of the organizations did not spend any of its \$9,900 contracted amount; the Office deobligated those funds and reallocated them to its capital improvement program.

Public Shelter Improvement Program. These funds are spent for emergency shelter renovation and improvement projects such as water and wastewater improvements; plumbing; restroom facilities; and electrical, communication, and heating and air conditioning systems.

The Office contracted with 9 communities and awarded \$430,000 of its community development program funds for this program. The communities had spent \$419,524 of these funds as of June 5, 2009; the Office deobligated unused funding of \$10,476 and reallocated the funds for other community development program uses.

Recommendations

The Office should:

- As it implements its new grants management system, develop a process to reconcile its grants management system to its accounting system.
- Continue to work with its contractors to address delays that have affected the rate at which Community Development Block Grant Program Round 2 hurricane recovery funds have been spent.

Management's Response

Recommendation:

As it implements its new grants management system, develop a process to reconcile its grants management system to its accounting system.

Management Response:

We agree with the recommendation.

As indicated in the initial SAO Audit Report 08-005 dated October 2007, the Office of Rural Community Affairs (ORCA) interfaces USAS payment data from its MIP Financial System to its Grant Contracts Management System. Financial staff verifies contract balances, expended amounts and remaining balances as part of the grant draw process. While these business processes provide reasonable assurance that grant contract balances are in agreement and "no" errors were discovered during the audit, we continue to agree that an ongoing reconciliation process is a prudent business process to implement

and as a result ORCA awarded a contract to Dulles Technologies implement a new Rural Grants Management System and assigned the agency's IRM to lead that effort.

Person responsible for implementation: Sharon Page, Chief Financial Officer.

Timeline: The planning and requirements definition phases of the implementation are under way and the deployment is scheduled to be completed before the end of fiscal year 2010.

Recommendation:

Continue to work with its contractors to address delays that have affected the rate at which Community Development Block Grant Round 2 hurricane recovery funds have been spent

Management Response:

We agree with the recommendation.

ORCA staff has worked extensively with the eight grantees awarded Round 2 hurricane recovery funds. While there have been delays on a few projects as a result of the 404 Army Corps of Engineers permitting process and the necessary acquisition of property to complete the projects, the Round 2 grants were awarded in Oct-Nov 2007 and are all within the initial two-year term of the contract period. Of the \$42 million awarded to grantees, over 34% has been expended and significant progress is expected in the next six months. It should be noted that efficiencies in the administration of these grant projects resulted in \$1.3 million (62%) of the general administration being freed up and made available for projects and construction. Two other projects will be completed under budget, which will also free up additional funds to be used for other hurricane recovery needs.

Person responsible for implementation: Oralia Cardenas, Director of Disaster Recovery Programs.

Timeline: Understanding that 404 Permits and acquisition of property is out of the control of the agency and in the hands of the grantee, the estimated completion date for Hurricane Rita Round 2 funds is December 2010.

Appendices

Appendix 1

Objectives, Scope, and Methodology

Objectives

The objectives of this audit were to:

- Determine the extent to which the Department of Housing and Community Affairs (Department) and the Office of Rural Community Affairs (Office) have implemented recommendations in *An Audit Report on Hurricane Recovery Funds Administered by the Department of Housing and Community Affairs and the Office of Rural Community Affairs* (State Auditor's Office Report No. 08-005, October 2007).
- Determine the amount of hurricane recovery funds the Department and the Office have spent.

Scope

The scope of this audit included following up on prior audit recommendations and covered all matters related to the administration of the two awards of Community Development Block Grant Program funds for hurricane recovery, as well as funds from other sources administered after September 1, 2005. The audit scope also included the automated systems and processes that support the functions being audited for Round 2 of Community Development Block Grant Program funds. Audit work related to automated systems unchanged from the prior audit was limited to determining the reliability of the information in the automated systems.

Methodology

The audit methodology included collecting information; conducting interviews with staff at the Department, the Office, councils of governments, selected contract administrators, and selected contract recipients; performing selected tests and procedures; and analyzing and evaluating the results of the tests.

Information collected and reviewed included the following:

- *State of Texas Action Plan for Community Development Block Grant Disaster Recovery Grantees under the Department of Defense Appropriations Act, 2006*, April 13, 2006 (prepared jointly by the Department and the Office).

- *Partial Action Plan for Disaster Recovery to Use Community Development Block Grant Funding to Assist with the Recovery of Distressed Areas Related to the Consequences of Hurricanes Katrina, Rita, and Wilma in the Gulf of Mexico in 2005*, April 13, 2007 (prepared by the Department).
- *Amendment to the Texas Action Plan for Disaster Recovery to Use Community Development Block Grant Funding to Assist with the Recovery of Distressed Areas Related to the Consequences of Hurricanes Katrina, Rita, and Wilma in the Gulf of Mexico in 2005*, approved by the Department's governing board on February 1, 2007 (prepared jointly by the City of Houston and Harris County).
- Department, Office, councils of governments, and contractor policies and procedures.
- Interviews with staff from the Department, the Office, councils of governments, contractors, and contract administrators.
- Data from automated systems at the Department, the Office, councils of governments, and contractors.
- Department, Office, councils of governments, and contractor's documents, including organizational charts, program implementation manuals, application files, expenditure files, contracts, environmental reviews and records, and correspondence via e-mail.
- *State of Texas Plan for Disaster Recovery U.S. Department of Housing and Urban Development (HUD), Consolidated Security, Disaster Assistance, and Continuing Appropriations Act, 2009*, March 4, 2009 (prepared by the Office).
- *Texas Rebounds, Helping our Communities Recover from the 2008 Hurricane Season*, November 2008 (prepared by the Office of the Governor).

Procedures and tests conducted included the following:

- Analyzed data from the accounting systems of the Department, the Office, councils of governments, and contractors.
- Analyzed information from the councils of governments and contractors' application management systems.
- Tested selected Department, Office, councils of governments, and contractor housing and non-housing application files to follow up on the implementation of prior audit recommendations and to ensure consistency

and compliance with federal and state rules, program requirements, and policies and procedures.

- Tested selected Department, Office, councils of governments, and contractor housing and non-housing expenditure files to ensure accuracy and allowability of expenditures.
- Analyzed data from the Department's contract management system.
- Analyzed contracts between the Department and the Office; the Department and the councils of governments; the Department and the contractor for the Homeowner Assistance Program and the Sabine Pass Restoration Program; the Department and the HOME Program contract administrators; the Office and the councils of governments; and the Office and contractors.
- Reviewed Department and Office monitoring procedures and monitoring reports.
- Confirmed the physical existence of 34 housing projects for the Community Development Block Grant Program and 27 housing projects for the HOME disaster recovery program.

Criteria used included the following:

- Code of Federal Regulations.
- Texas Statutes and the Texas Administrative Code.
- U.S. Office of Budget and Management circulars.
- Department, Office, councils of governments, and contractor policies and procedures.
- Contract provisions.
- Public Laws 109-148, 109-234, and 110-329.
- U.S. Code.

Project Information

Audit fieldwork was conducted from March 2009 through June 2009. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The following members of the State Auditor's staff performed the audit:

- Jennifer Lehman, MBA, CGAP (Project Manager)
- David E. Dowden (Assistant Project Manager)
- Carl Ela
- Robert Pagenkopf
- Mary Ann Wise, CPA, CFE
- Brian York
- Marlen Randy Kraemer, MBA, CGAP, CISA (Information Systems Audit Team)
- Rachelle Wood, MBA, CISA (Information Systems Audit Team)
- Charles P. Dunlap, CPA (Quality Control Reviewer)
- J. Scott Killingsworth, CIA, CGAP, CGFM (Quality Control Reviewer)
- Michael Apperley, CPA (Assistant State Auditor)

Time Line for and Availability of the Department of Housing and Community Affairs' Hurricane Recovery Funds

Table 7 provides information on the time line for and availability of the Department of Housing and Community Affairs' (Department) hurricane recovery funds for Hurricane Katrina and Hurricane Rita.

Table 7

Time Line for and Availability of the Department's Hurricane Recovery Funds for Hurricane Katrina And Hurricane Rita	
Date	Event
August 2005	Hurricane Katrina makes landfall in Louisiana.
September 2005	Hurricane Rita makes landfall in Texas.
December 2005	The Department releases a notice of funding availability for approximately \$1.8 million in Housing Trust Funds for disaster recovery through Bootstrap Program contracts.
January 2006	The Department releases a notice of funding availability for \$8,300,000 in HOME Program funds for disaster recovery efforts.
March 2006	The Department awards contracts to HOME Program contract administrators for the \$8,300,000 allocation. The Department awards two contracts for Bootstrap Program disaster recovery funds.
May 2006	The U.S. Department of Housing and Urban Development (HUD) approves the Texas Action Plan for Round 1 of Community Development Block Grant Program funds and makes \$74,523,000 available to Texas. Of that amount, \$42,378,185 is made available to the Department for housing activities.
June 2006	The Department awards one contract for Bootstrap Program funds.
July 2006	The Department releases a notice of funding availability for \$4,200,000 in HOME Program funds for disaster recovery efforts. The Department's Board approves the council of governments' method of distribution for Round 1 of Community Development Block Grant Program funds. The Department executes contracts with three councils of governments to administer Round 1 of Community Development Block Grant Program funds.
September 2006	The South East Texas Regional Planning Commission begins working with the Department and HUD on the environmental review process.
October 2006	The Department awards contracts to HOME Program contract administrators for the \$4,200,000 allocation. The South East Texas Regional Planning Commission publishes a "Notice of Intent to Request Release of Funds" for Round 1 of Community Development Block Grant Program funds.
November 2006	HUD authorizes the South East Texas Regional Planning Commission to use Round 1 Community Development Block Grant Program funds.
February 2007	The Deep East Texas Council of Governments publishes a "Notice of Intent to Request Release of Funds" for Round 1 of Community Development Block Grant Program funds.
March 2007	The Houston-Galveston Area Council publishes a "Notice of Intent to Request Release of Funds" for Round 1 of Community Development Block Grant Program funds.

**Time Line for and Availability of the Department's
Hurricane Recovery Funds for Hurricane Katrina And Hurricane Rita**

Date	Event
April 2007	<p>HUD makes \$365,671,843 in Round 2 Community Development Block Grant Program funds available for activities described in the Texas Action Plan. Of that amount, \$321,571,849 is made available to the Department for housing activities.</p> <p>The Department releases a notice of funding availability for \$82,867,166 in Round 2 Community Development Block Grant Program funds for the Rental Housing Stock Restoration Program.</p> <p>HUD authorizes the Deep East Texas Council of Governments and the Houston-Galveston Area Council to use Round 1 of Community Development Block Grant Program funds.</p>
August 2007	<p>The Department's Board approves the selection of ACS, Inc. (ACS) to administer the Homeowner Assistance Program and Sabine Pass Restoration Program for Round 2 of Community Development Block Grant Program funds.</p> <p>HUD approves an amendment to the partial action plan for Round 2 of Community Development Block Grant Program funds and makes \$63,000,000 available to the City of Houston and Harris County.</p> <p>The Department executes contracts with the City of Houston and Harris County to administer Round 2 of Community Development Block Grant Program funds.</p>
September 2007	<p>The Department's Board approves seven contractors for Round 2 of Community Development Block Grant Program funds for the Rental Housing Stock Restoration Program.</p> <p>The Department deobligates funds from one of the HOME Program disaster recovery contracts due to inability to identify qualified applicants.</p>
December 2007	<p>The Department executes a contract with ACS to administer Round 2 Community Development Block Grant Program funds for the Homeowner Assistance Program and the Sabine Pass Restoration Program. ACS sub-contracts with Reznick Group and Shaw Environmental and Infrastructure, Inc.</p> <p>The Department deobligates funds from one of the HOME Program disaster recovery contracts due to inability to identify qualified applicants.</p>
January 2008	<p>The Department deobligates funds from one of the disaster recovery contracts of the Bootstrap Program due to poor performance.</p>
March 2008	<p>ACS and its sub-contractor Shaw Environmental and Infrastructure, Inc. begin working with the Department and HUD on the environmental assessment review process for Round 2 Community Development Block Grant Program funds for the Sabine Pass Restoration Program.</p>
April 2008	<p>ACS and its sub-contractor Shaw Environmental and Infrastructure, Inc. begin working with the Department and HUD on the environmental assessment review process for Round 2 Community Development Block Grant Program funds for the Homeowner Assistance Program.</p>
May 2008	<p>The Department and the South East Texas Regional Planning Commission begin work to complete the environmental assessment for Round 1 of Community Development Block Grant Program funds.</p> <p>The Department deobligates funds from another of the disaster recovery contracts of the Bootstrap Program due to poor performance.</p>
July 2008	<p>ACS and its sub-contractor Shaw Environmental and Infrastructure, Inc. publish a combined "Finding of No Significant Impact/Notice of Intent to Request Release of Funds" for Round 2 of Community Development Block Grant Program funds for the Sabine Pass Restoration Program.</p> <p>The South East Texas Regional Planning Commission publishes a combined "Finding of No Significant Impact/Notice of Intent to Request Release of Funds" for Round 1 of Community Development Block Grant Program funds.</p>

Time Line for and Availability of the Department's Hurricane Recovery Funds for Hurricane Katrina And Hurricane Rita	
Date	Event
August 2008	HUD authorizes the South East Texas Regional Planning Commission to use Round 1 of Community Development Block Grant Program funds.
September 2008	HUD authorizes ACS to use Round 2 of Community Development Block Grant Program funds for the Sabine Pass Restoration Program. Hurricane Ike makes landfall in Texas.
November 2008	The Department sends questions to HUD to clarify courses of action for determining duplication of benefits for damages caused by both Hurricane Rita and Hurricane Ike.
December 2008	ACS and its sub-contractor Shaw Environmental and Infrastructure, Inc. publish a combined "Finding of No Significant Impact/Notice of Intent to Request Release of Funds" for the South East Texas Regional Planning Commission and the Houston-Galveston Area Council areas for Round 2 of Community Development Block Grant Program funds for the Homeowner Assistance Program. The Department deobligates funds from the final disaster recovery contract of the Bootstrap Program due to poor performance.
January 2009	ACS and its sub-contractor Shaw Environmental and Infrastructure, Inc. publish a combined "Finding of No Significant Impact/Notice of Intent to Request Release of Funds" for Round 2 of Community Development Block Grant Program funds for the Deep East Texas Council of Governments area for the Homeowner Assistance Program. HUD authorizes ACS to use Round 2 of Community Development Block Grant Program funds for the South East Texas Regional Planning Commission area for the Homeowner Assistance Program.
February 2009	HUD authorizes ACS to use Round 2 of Community Development Block Grant Program funds for the Houston-Galveston Area Council and the Deep East Texas Council of Governments areas for the Homeowner Assistance Program.
March 2009	HUD provides responses to the Department on courses of action for determining duplication of benefits for damages caused by both Hurricane Rita and Hurricane Ike.

Sources: Department information; the *Texas Action Plan for Hurricane Rita* (April 2006); the *Texas Rebounds Report* (November 2008), and environmental assessment documentation for Round 2 of Community Development Block Grant Program funds for the Sabine Pass Restoration Program and the Homeowner Assistance Program prepared by Shaw Environmental and Infrastructure, Inc.

Information Regarding Recovery Funds for Hurricane Ike

The following information was summarized from:

- *Texas Rebounds, Helping Our Communities Recover from the 2008 Hurricane Season*, November 2008, Office of the Governor.
- Consolidated Security, Disaster Assistance, and Continuing Appropriations Act, 2009; Public Law 110-329.
- *State of Texas Plan for Disaster Recovery*; March 4, 2009; Office of Rural Community Affairs.

Background Information

Hurricane Ike made landfall in Texas on September 13, 2008. Thirty-eight Texas counties were subsequently designated as presidentially declared disaster areas. Preliminary, unreimbursed damages from the 2008 hurricane season were estimated at \$29.4 billion.

Source: *Texas Rebounds, Helping Our Communities Recover from the 2008 Hurricane Season*, November 2008, Office of the Governor.

To assist in recovery from Hurricane Ike, the U.S. Department of Housing and Urban Development (HUD) will provide Texas with \$1,314,990,193 in disaster recovery supplemental funds from the Community Development Block Grant Program for necessary expenses related to disaster relief; long-term recovery; and restoration of infrastructure, housing, and economic revitalization. HUD allocated these funds to the State in November 2008 through the \$6,053,584,933 in Community Development Block Grant Program funds made available through the U.S. Consolidated Security, Disaster Assistance, and Continuing Appropriations Act, which was enacted on September 30, 2008. On June 10, 2009, HUD announced that the State will receive an additional \$1,743,001,247 in assistance. This appendix discusses plans for the initial \$1,314,990,193 amount as included in the action plan developed by the Office of Rural Community Affairs (Office).

Governor Rick Perry designated the Office as the entity responsible to HUD for the administration of these funds. The Department of Housing and Community Affairs (Department) will administer the portion of the funds designated for housing. The primary method of allocating funds to affected regions in the State was based on damage assessment data provided by the Federal Emergency Management Agency (FEMA). Allocation amounts were provided to 11 council of governments regions in which damage occurred. Of the initial \$1,314,990,193 allocated to Texas, the State has set aside:

- \$65,749,510 (5.00 percent) for state administrative expenses.
- \$36,559,240 (2.78 percent) for planning activities.
- \$58,834,914 (4.47 percent) for the Department's Affordable Rental Housing Stock Restoration Program.

The remaining \$1,153,846,529 (87.75 percent) will be distributed to the 11 council of governments regions. Table 8 specifies the amounts and percentages allocated to each council of governments region.

Table 8

Allocation of Funds for Recovery from Hurricane Ike		
Council of Governments Region	Amount Allocated to Region	Percent Allocated to Region ^a
Houston-Galveston Area Council	\$ 814,133,493	70.56%
South East Texas Regional Planning Commission	190,000,000	16.47%
Deep East Texas Council of Governments	70,000,000	6.07%
Lower Rio Grande Valley Development Council	55,000,000	4.77%
East Texas Council of Governments	9,224,823	0.80%
Brazos Valley Council of Governments	8,952,164	0.78%
Coastal Bend Council of Governments	3,121,376	0.27%
Ark-Tex Council of Governments	1,164,673	0.10%
Golden Crescent Regional Planning Commission	1,000,000	0.09%
South Texas Development Council	1,000,000	0.09%
Central Texas Council of Governments	250,000	0.02%
Total	\$1,153,846,529	100.00%

^a Percentages do not sum precisely due to rounding.

Source: *State of Texas Plan for Disaster Recovery, U.S. Department of Housing and Urban Development (HUD), Consolidated Security, Disaster Assistance, and Continuing Appropriations Act, 2009*, March 4, 2009, prepared by the Office. Note: percentages were calculated by auditors.

The Office will require each of the 11 regions to define its method of funds distribution in a uniform format provided by the Office. Each council of governments must determine the method of distribution for the region, including specifying what portions of the funds will be used for housing and non-housing activities. The Office will provide the councils of governments with method of distribution forms, form guidelines, detail worksheets, and worksheet samples. The method of distribution guidelines require that each council of governments hold at least two public hearings prior to completion of the method of distribution form.

The councils of governments will establish their methods of distribution and the Office will approve them. The regional funding parameters in the methods of distribution will guide the use of the funds. Applications will then be developed based on the eligible activities in each region.

An action plan developed by the Office with input from FEMA, the Office of the Governor, local government officials, and other parties requires the State to spend \$139,743,911 (10.6 percent of the initial \$1,314,990,193 allocation)

for affordable rental housing programs. The State will meet part of this requirement with the \$58,834,914 set-aside for the Department's Rental Housing Stock Restoration Program. The remaining \$80,908,997 that must be spent on affordable rental housing programs will be allocated by the councils of governments.

Funds will be awarded to eligible subrecipients for their use in carrying out agreed-upon housing program activities in their prospective regions. Subrecipients may include cities, counties, councils of governments, and private non-profit organizations. Funds will be granted only to eligible subrecipients that have the capacity to carry out the housing activities in their applications and in accordance with their contracts with the Department.

To expedite the expenditure, use, and recovery of program funds (where provided for), contract terms with entities receiving grant funds will generally not exceed two years. The Office and the Department will have the ability to grant contract extensions.

Management Response from the Department



TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS

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July 24, 2009

State Auditor's Office
P. O. Box 12067
Austin, Texas 78711-2067

Attention: Jennifer Lehman

Re: TDHCA Management Response to Draft Audit on Disaster Recovery

Dear Ms. Lehman:

Management and staff of the Texas Department of Housing and Community Affairs (TDHCA) appreciate the work performed by the State Auditor's Office (SAO) in your audit of our disaster recovery programs. The entire audit team was very professional, capable, and diligent. Their assessment will help us to continue to manage these programs efficiently and effectively.

Specifically, there are a number of items reflected in the report that illustrate that we are succeeding in our commitment to administering these funds with the least possible risk. Specifically, the audit:

- Identified no issues in the reliability and completeness of data;
- Tested 90 application files at the Councils of Government and determined that income calculations were performed correctly for all 90;
- Tested 43 application files at ACS (TDHCA's prime contractor for the administration of Hurricane Rita Round II funding) and determined that income calculations were performed correctly for all 43;
- Determined that all HOME disaster contracts were set up after the environmental clearances were complete, as required by HUD rules;
- Tested 30 HOME disaster contract draws and determined that all 30 were allowable draws for which TDHCA had validated costs; and
- Tested 30 HOME disaster contract files and determined that all 30 included the applicants' signatures on all contract documentation as required.

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We are also proud of the fact that we have made great strides, especially in recent months, in expanding the construction activity and expediting the delivery of needed replacement housing. Under Hurricane Rita, round II funding, as of today there were 650 homes actively under construction and 145 homes completed.

Below are the requested management responses to specific items identified in the report.

Chapter 1-A

SAO Recommendation

The Department should continue to work toward addressing delays that have affected the rate at which Community Development Block Grant hurricane recovery funds have been spent.

Management Response

Management agrees with the recommendation. However, the streamlining suggested by the SAO must be a coordinated effort among a number of federal, state, and local governmental entities, and significant streamlining may not be possible without changes to federal and state laws governing the Community Development Block Grant program.

Disaster response is an urgent need, and where processes can be streamlined or accelerated to bring needed relief more quickly, such improvements will be made. However, they must always be made in a manner that minimizes the risk of fraud, waste, and abuse and provides assurance that these public funds are, in fact, used only to build safe, decent homes for qualified individuals.

During the 81st legislative session, the Legislature provided additional guidance to the Department in order to expedite disaster relief even where recipients could not document legal title to their homes. The Department's Governing Board consequently adopted a policy to move forward with providing relief to these individuals. The Department has worked proactively with ACS, the COGs, and other parties to streamline these processes wherever possible and will continue to seek opportunities to address any delays.

Person Responsible: *Kelly Crawford*

Target Date for Implementation: *September 1, 2009*

Chapter 1-E

SAO Recommendation

The Department should ensure that its contractor strengthens information technology controls related to the administration of hurricane recovery funds.


Management Response

Management agrees with the recommendation and will work with ACS to ensure that their information technology controls are strengthened. TDHCA's Information Technology staff and Disaster Recovery & Emergency Housing staff will meet with ACS and ensure that the necessary measures are taken and that the recommended controls are implemented.

Person Responsible: *Curtis Howe*
Target Date for Implementation: *September 1, 2009*

The Department's management and staff again extend our thanks to the SAO for its efforts. We would like to emphasize our commitment to managing our disaster recovery resources as efficiently as possible while maintaining the necessary level of control to ensure that all expenditures are allowable and are properly documented. Please contact me or Sara Newsom, Deputy Executive Director Disaster Recovery and Emergency Housing, if there are any questions or if we can be of further assistance.

Sincerely,



Michael Gerber
Executive Director

cc:

Sandy Donoho, Director of Internal Audit
Sara Newsom, Deputy Executive Director for Disaster Recovery and Emergency Housing
Kelly Crawford, Director for Disaster Recovery and Emergency Housing
Tim Irvine, Chief of Staff

Management Response from the Office



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July 27, 2009

Jennifer Lehman, Senior Auditor
Texas State Auditor's Office
1501 N. Congress Ave.
Austin, TX 78701

Dear Ms. Lehman:

In response to the issues raised in the follow up audit Report No. 08-005, please find the responses from the Office of Rural Community Affairs below:

Recommendation:

As it implements its new grants management system, develop a process to reconcile its grants management system to its accounting system.

Management Response:

We agree with the recommendation.

As indicated in the initial SAO Audit Report 08-005 dated October 2007, the Office of Rural Community Affairs (ORCA) interfaces USAS payment data from its MIP Financial System to its Grant Contracts Management System. Financial staff verifies contract balances, expended amounts and remaining balances as part of the grant draw process. While these business processes provide reasonable assurance that grant contract balances are in agreement and “no” errors were discovered during the audit, we continue to agree that an ongoing reconciliation process is a prudent business process to implement and as a result ORCA awarded a contract to Dulles Technologies implement a new Rural Grants Management System and assigned the agency’s IRM to lead that effort.

Person responsible for implementation: Sharon Page, Chief Financial Officer.

Timeline: The planning and requirements definition phases of the implementation are under way and the deployment is scheduled to be completed before the end of fiscal year 2010.

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Charles S. (Charlie) Stone
ORCA Executive Director

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Vernon: 940-553-3556

Recommendation:

Continue to work with its contractors to address delays that have affected the rate at which Community Development Block Grant Round 2 hurricane recovery funds have been spent

Management Response:

We agree with the recommendation.

ORCA staff has worked extensively with the eight grantees awarded Round 2 hurricane recovery funds. While there have been delays on a few projects as a result of the 404 Army Corps of Engineers permitting process and the necessary acquisition of property to complete the projects, the Round 2 grants were awarded in Oct-Nov 2007 and are all within the initial two-year term of the contract period. Of the \$42 million awarded to grantees, over 34% has been expended and significant progress is expected in the next six months. It should be noted that efficiencies in the administration of these grant projects resulted in \$1.3 million (62%) of the general administration being freed up and made available for projects and construction. Two other projects will be completed under budget, which will also free up additional funds to be used for other hurricane recovery needs.

Person responsible for implementation: Oralia Cardenas, Director of Disaster Recovery Programs.

Timeline: Understanding that 404 Permits and acquisition of property is out of the control of the agency and in the hands of the grantee, the estimated completion date for Hurricane Rita Round 2 funds is December 2010.

Let me say that you and your staff have been very cordial and accommodating during this audit. Please let me know if you have any questions or concerns about the responses outlined in this letter.

Sincerely,



Charles S. (Charlie) Stone
Executive Director

Related State Auditor's Office Work

Related SAO Work		
Number	Product Name	Release Date
08-005	An Audit Report on Hurricane Recovery Funds Administered by the Department of Housing and Community Affairs and the Office of Rural Community Affairs	October 2007

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