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United States General Accounting Office
Washington, DC 20548

May 11, 2001

The Honorable Mel Martinez
The Secretary of Housing
and Urban Development

Subject: *Status of GAO's Recommendations to the Department of Housing and Urban Development*

Dear Mr. Secretary:

We appreciated meeting with you earlier this year to discuss the management challenges facing the Department of Housing and Urban Development (HUD). As I mentioned in our meeting, we have issued several reports containing recommendations for improving various aspects of HUD's programs and operations. During the meeting, you said that you would appreciate receiving a summary of HUD's progress in implementing our recommendations. This letter summarizes our understanding of HUD's progress implementing our key open recommendations. The enclosure contains a complete update of the status of all open recommendations. Most of these recommendations were made in reports issued in 1999 and 2000, although some are based on a report issued in 1994.

HUD officials have reported to us that they are making progress in addressing many of the open recommendations, although in some cases considerable work still must be done before we can consider them implemented. The enclosure, which lists the status of our open recommendations, reflects a reduction of 19 recommendations that we have closed due to HUD actions since our September 2000 update and the addition of four new recommendations from recently issued products.

This letter focuses on the status of nine of the recommendations that we consider to be key recommendations because of the impact they can have on managing HUD's programs. As you know, our January 2001 Performance and Accountability Series provides an overview of where HUD currently stands on management issues. In that report we note that HUD has taken important steps toward addressing some of its management deficiencies; however, significant weaknesses still persist in some of HUD's major program areas, including single-family mortgage insurance, rental housing assistance, information and financial management systems, and human capital.¹ Seven of the nine key recommendations deal with two of the performance and accountability areas, single-family mortgage insurance and information and financial management systems. We are also including two recommendations dealing with HUD's budget process because we believe their implementation is critical to getting a better handle on HUD's management issues. In many cases we are consulting with your staff as HUD implements the recommendations.

¹ See *Major Management Challenges and Program Risk: Department of Housing and Urban Development* (GAO-01-248, Jan. 2001)

Improved Single-Family Mortgage Insurance Management Can Reduce Financial Risks

HUD's internal controls over its single-family mortgage insurance programs do not adequately promote effective monitoring of contractors, lenders, and appraisers or ensure the integrity of the loan origination process. Recommendations in the single-family mortgage insurance area that we believe are in need of your priority attention and their status follow:

- In May 2000,² we recommended that HUD develop methods to encourage contractors to reduce the number of single-family properties that have been in inventory longer than 6 months. HUD officials report that they have amended management and marketing contracts to address the long-standing problems of inadequate property maintenance. These actions, however, do not address the need to provide tools, such as incentives and penalties, to ensure that the contractors aggressively market the less saleable properties and remove any impediments that cause them to stay in the inventory. We will keep this recommendation open until HUD has developed controls that specifically address the aged inventory problem.
- In April 2000,³ we recommended that, once the legal basis of the Credit Watch Program is resolved, HUD revise the Credit Watch Program's regulations to cover lenders that sponsor other lenders as loan correspondents and underwrite the loans that the correspondents originate. Currently, HUD's Credit Watch Program is designed to identify and terminate the loan origination authority of lenders with a high ratio of loan defaults, but is silent with regard to lenders who underwrite the loans of their correspondents. HUD officials told us that they believe legislative changes to the National Housing Act are needed for the department to take action against lenders that sponsor loan correspondents with unacceptable loan default rates. In its 2002 budget submission, HUD included an amendment to the National Housing Act expanding the Secretary's authority to include originators and underwriters of loans. We will keep this recommendation open pending the outcome of the legislative proposal.
- In April 1999,⁴ we recommended that HUD determine the department's authority to hold FHA-approved lenders accountable for poor-quality FHA appraisals performed by the appraisers they select and issue policy guidance that sets forth the specific circumstances under which HUD may exercise its authority to hold lenders accountable. HUD informed us that it is working on a letter to mortgagees that it believes will meet our recommendations. We will keep this recommendation open pending our review of the mortgagee letter.
- Recently, in a February 2001 report,⁵ we recommended that HUD develop criteria for measuring the actuarial soundness of the Mutual Mortgage Insurance Fund. Under this Fund, HUD's FHA provides insurance for private lenders against losses on home mortgages. The criteria should specify the economic conditions that the Fund would be expected to withstand and may specify capital ratios currently consistent with these

² See *Single-Family Housing: Stronger Measures Needed to Encourage Better Performance by Management and Marketing Contractors* (GAO/RCED-00-117, May 12, 2000).

³ See *Single-Family Housing: Strong Oversight of FHA Lenders Could Reduce HUD's Insurance Risk* (GAO/RCED-00-112, Apr. 28, 2000). Subsequent to our report, the U. S. Court of Appeals held that the Credit Watch Program's termination regulations were valid in Capitol Mortgage Bankers, Inc. v. Cuomo, 222 F. 3d 151 (4th Cir. 2000).

⁴ See *Single-Family Housing: Weaknesses in HUD's Oversight of the FHA Appraisal Process* (GAO/RCED-99-72, Apr. 16, 1999).

⁵ See *Mortgage Financing: FHA's Fund Has Grown, but Options for Drawing on the Fund Have Uncertain Outcomes* (GAO-01-460, Feb. 28, 2001).

criteria. In addition, HUD's annual actuarial reviews should give more attention to tests of the Fund's ability to withstand appropriate stresses, including more severe scenarios that capture worse-than-expected loan performance that may result from economic changes and other factors. HUD has not yet responded to this recently issued report.

More Effective Information and Financial Systems Would Improve Management Oversight

We have been working with HUD officials to resolve a range of information technology management issues. Our open recommendations in this area date back to our April 1994 report⁶ on HUD's information resources management program. For example:

- In April 1994, we recommended that HUD develop and test contingency plans (business resumption plans) for the backup, recovery, and continuity of operations of all systems and computer installations that support critical departmental functions. Without adequate contingency plans, HUD faced unnecessarily high risks that its missions would be seriously impaired if a major service disruption or disaster occur. HUD has developed contingency plans. However, in its reports on HUD's fiscal years 1999 and 2000 financial statements, HUD's Office of Inspector General noted testing deficiencies that constituted serious internal control weaknesses. Because this concerns HUD's ability to perform critical functions and support critical programs in the aftermath of a major disruption or disaster, we will keep this recommendation open until the plans have been tested adequately and HUD makes provisions to ensure the plans are sufficiently being tested on an ongoing basis.
- In April 1994, we also recommended that HUD improve its computer security controls because the security weaknesses we observed posed risks to the integrity of the department's computer systems and sensitive data. In addition, our April 1999 report⁷ on four HUD grant programs disclosed that HUD still could not show that only authorized users were accessing its computer systems. HUD has made progress in both of these areas. However, HUD's Inspector General continues to report serious weaknesses in computer security. The Inspector General's March 1, 2001, report on HUD's fiscal year 2000 financial statements again discusses serious computer security deficiencies. These deficiencies include the lack of automated system security, computer and data access controls, and background investigations of staff with access to sensitive systems or data--the same deficiencies we observed and reported in 1994. We will keep this recommendation open until these deficiencies are corrected.
- Our 1994 report also recommended that HUD develop and link strategic business and information resources management planning processes. We also recommended that HUD develop a departmentwide enterprise architecture to establish a standard framework for guiding the management and use of information management resources to accomplish HUD's mission and objectives. Without strategic business and information resource management planning, HUD did not have a sound basis for developing a departmentwide enterprise architecture. HUD has articulated a business vision in its 20/20 reform plan and annual Government Performance and Results Act plans and has also reported completing a baseline enterprise architecture in January 2001. The department still needs to better align its strategic business and information resource management plans and integrate the plans with its capital investment management processes before we can

⁶ See *HUD Information Resources: Strategic Focus and Improved Management Controls Needed* (GAO/AIMD-94-34, Apr. 14, 1994).

⁷ See *Community Development: Weak Management Controls Compromise Integrity of Four HUD Grant Programs* (RCED-99-98, Apr. 27, 1999).

close the planning recommendation. We will examine HUD's recently completed baseline enterprise architecture and its implementation to determine whether it results in a departmentwide standard framework for guiding the management and use of information resources.

Better Management of Unexpended Budget Balances Would Improve Program Operations

For years, unexpended balances have clouded HUD's budget needs because HUD has not adequately determined what portion of them is available for recapture. While these balances have been very large, HUD has not had the information needed to quantify the portion that could be used to offset the need for new appropriations. We made the following recommendations to address these issues:

- In September 1999,⁸ we concluded that HUD could better manage unexpended balances in its larger grant programs and some unobligated funding could be used to meet other needs. We recommended that HUD's Office of Budget work with HUD's program offices to identify programs with a history of unobligated balances, as well as grantees holding excessive balances, so that action could be taken to ensure the expeditious obligation and expenditure of these funds. In response, HUD has established a departmental task force and contracted with three contractors to review programs carrying large balances, including HUD's Section 202, Public Housing Capital Fund, Community Development Block Grant, and Section 8 tenant-based programs. However, the task force has not been institutionalized within HUD, and the contracted studies have not been completed. We will keep this recommendation open until we are satisfied that HUD is effectively managing its unexpended balances.
- In April 2001 testimony,⁹ we reported that without accurate and timely information about the nature, amount, and availability of HUD's unexpended balances, decisionmakers could not fully and fairly evaluate the department's funding needs. In order for HUD to fully account for unexpended balances in its funding requests, we recommended that the Secretary (1) develop systems that routinely provide timely, reliable information on the status of unexpended funds for the purpose of quantifying the amount available for recapture or rescission; (2) routinely incorporate this information into the management and operations of programs, and (3) consistently use this information in formulating its budget request, clearly demonstrating how it is taking these balances into account when setting forth its budget needs. HUD has not yet responded to this recent recommendation.

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We typically update the status of our open recommendations annually. Sometimes this process is complicated by differences in our view and those of HUD staff on whether our recommendations have been fully implemented. For example, when a recommendation has more than one part and HUD has implemented some but not all of the parts, HUD may believe that the recommendation should be closed. However, we will not fully close out a recommendation until we are satisfied that all key parts of that recommendation are met. In addition, in some cases, HUD reports to us that it has developed reform plans or a draft proposal to fix a problem. While such initiatives are important, we do not believe that reform plans or draft documents alone are sufficient for us to close out a recommendation. Rather,

⁸ See *HUD's Fiscal Year 2000 Budget Request: Additional Analysis and Justification Needed for Some Programs* (GAO/RCED-99-251, Sept. 3, 1999).

⁹ See *Comments on HUD's Fiscal Year 2002 Budget Request* (GAO-01-663T, Apr. 25, 2001).

it is the results of such reform initiatives that demonstrate management problems have been corrected that count.

We look forward to consulting with your staff to help them implement these recommendations. It was a pleasure meeting with you on these important issues. Please feel free to contact me at (202) 512-7631 or Bob Procaccini at (202) 512-6776 if you have any questions concerning this letter or about the status of our recommendations. Key contributors to this report are Angela Davis and Andy Finkel.

Sincerely yours,

A handwritten signature in black ink that reads "Stanley J. Czerwinski". The signature is written in a cursive, flowing style.

Stanley Czerwinski
Director, Physical Infrastructure Issues

Enclosure

Enclosure: Status of GAO's Open Recommendations to the Department of Housing and Community Development

GAO Report	Recommendation	Status	Contacts
AIMD -94-34			
HUD Information Resources: Strategic Focus and Improved Management Needed (04/14/94)	develop and test contingency plans for the backup, recovery, and continuity of operations of all systems and computer installations that support critical departmental functions. Until the plans are fully developed and tested, report the lack of contingency plans as a material internal control weakness.	Open, pending clean Inspector General opinion on a fully tested contingency plan	GAO - Dave Gill 512-6250 HUD - Mike Milazzo 708-0220 x6098
	eliminate weaknesses in computer security controls over automated systems and installations that store, process, transmit, or use sensitive or privacy data. This will require establishing effective mechanisms to ensure that both HUD and HUD contractor (1) computer operations conform with federal and departmental requirements, (2) staffs receive appropriate background investigations that are commensurate with their access to sensitive systems, and (3) staffs receive sufficient computer security training so that they are aware of and can fulfill their computer security responsibilities.	Open, pending HUD action	GAO - Dave Gill 512-6250 HUD - Holloway Coats 708-0614 x6006 or Pam Woodside 708-0614 x109
	establish strategic business and IRM planning processes and develop and maintain plans that are clearly linked to each other. The plans should articulate senior executive's vision of the mission, objectives, and priorities.	Open, pending our review of recent HUD activity	GAO- Dave Gill 512-6250 HUD - Debra Stouffer 708-2374 x108
	...develop an enterprise architecture based on the strategic business and IRM plans to govern the development, deployment, and use of IRM resources	Open, pending our review of recent HUD activity	GAO- Dave Gill 512-6250 HUD - Debra Stouffer 708-2374 x108
AIMD-99-25			
HUD Information Systems: Improved Management Practices Needed to Control Integration Cost and Schedule (12/18/1998)	...ensure that the department develops and uses defined processes for estimating information technology project costs, including Software Engineering Institute requisites	Open pending HUD implementation of its planned fixed price, outcome-based contract system	GAO - Dave Gill 512-6250 HUD - Dennis Peacock 708-0614 x6285

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	ensure that the department fully implements and institutionalizes a disciplined and documented information technology investment management process consistent with provisions of the Clinger-Cohen and Paperwork Reduction Acts and GAO and OMB's guidance for selecting, controlling, and evaluating information technology investments	Open, pending our review of recent HUD activity	GAO - Dave Gill 512-6250 HUD - Debra Stouffer 708-2374 x108
RCED-99-251			
HUD's Fiscal Year 2000 Budget Request: Additional Analysis and Justification Needed for Some Programs (09/3/99)	direct the Office of Budget to work with HUD's program offices to identify programs with a history of unobligated and undisbursed balances, as well as grantees holding excessive balances, so that action can be taken to ensure the expeditious obligation and expenditure of these funds	Open, pending HUD's completion of ongoing and future reviews of unobligated balances	GAO - Carol Anderson-Guthrie 214 777-5739 HUD - Ronald Spraker 708-2865 x6851
	establish firm monitoring procedures for overseeing multifamily housing contract administrators' performance and property condition, and amend its budget request to reflect the reduced scope from the exclusion of certain properties in the program	Open, pending final approved monitoring procedures	GAO - Carol Anderson-Guthrie 214 777-5739 HUD - Ronald Spraker 708-2865 x6851
RCED-99-98			
Community Development: Weak Management Controls Compromise Integrity of Four HUD Grant Programs (04/27/99)	...consider whether it is more cost-effective to modify IDIS or replace it....ensure that a new system corrects the problems GAO found with IDIS	Open, pending implementation of effective new grants management system	GAO- Frank Minore 512-7639 HUD - Bill Eargle 708-2186 x3844

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	regardless of the decision on the future of IDIS....ensure that access to IDIS is limited to authorized users and that those users have access levels appropriate to the duties they perform....ensure that the security officer for IDIS is fully aware of the responsibilities that must be carried out and has the appropriate training and staff for those responsibilities	Open, pending appropriate HUD action	GAO- Frank Minore 512-7639 HUD - Bill Eargle 708-2186 x3844
RCED 00-31			
Multifamily Housing: Impact of Loan Sales on Tenants and Properties Varies by Property (01/20/00)	determine whether four properties violated the prohibition against discrimination; and if so, take appropriate enforcement action	Open, pending referral to HUD's enforcement center for final resolution	GAO - Jim Vitarello 512-5119 HUD - Jim Mitchell 708-3703
	notify housing authorities and assisted tenants associated with partially assisted loan sale properties of the tenant protections and of their rights to seek judicial enforcement of these protections	Open, pending distribution of HUD letter to individual public housing authorities	GAO - Jim Vitarello 512-5119 HUD Audrey Hinton 708-2866 x2691
	follow up with housing authorities to determine whether they are able to enforce the tenant protections or whether further steps are needed to enforce the protections	Open, pending distribution of HUD letter to individual public housing authorities	GAO - Jim Vitarello 512-5119 HUD Audrey Hinton 708-2866 x2691
AIMD-00-60R			
Credit Reform: HUD's FY 2000 Credit Subsidy Estimates Were Reasonable, But Could Have Been Improved	use the audited liability for loan guarantees model when preparing the President's budget submission for the MMI fund. In the interim, complete the detailed cell-by-cell review of the budget model to identify and correct all formula errors.	Open, pending HUD action	GAO - Dan Blair 512-9401 HUD – Judy May 401-0450 x3239
	establish a supervisory review process detailed enough to identify formula errors in budget models prior to submitting credit subsidy estimates to OMB for inclusion in the President's budget	Open, pending HUD action	GAO - Dan Blair 512-9401 HUD – Judy May 401-0450 x3239

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	implement plans to adjust the timing of audit procedures related to credit subsidies so that these procedures are completed in time for any alternate sources of data and errors found are factored into the President's budget submission	Open, pending HUD action	GAO - Dan Blair 512-9401 HUD – Judy May 401-0450 x3239
	improve HUD's credit estimation process by establishing a process to incorporate all necessary revisions identified during the audit in time to meet the schedule for the President's budget submission	Open, pending HUD action	GAO - Dan Blair 512-9401 HUD – Judy May 401-0450 x3239
GGD-98-48			
GSE's: Federal Oversight Needed for Nonmortgage Investments	develop criteria through appropriate rulemaking processes to help ensure that the housing enterprises' nonmortgage investments are consistent with the purposes expressed in their charter acts	Open, pending final rule	GAO- Bill Shear 512-4325 HUD - Sandra Fostek 708-2224
RCED-00-112			
Single-Family Housing: Strong Oversight of FHA Lenders Could Reduce HUD's Insurance Risk (04/28/00)	revise the Credit Watch Program's regulations to cover lenders that underwrite FHA-insured loans with excessive default and claim rates as well as those lenders that originate such loans	Open, pending legislation	GAO - Stan Ritchick 512-6788 HUD - Phil Murray 708-1515
	develop procedures and enhance FHA's management information systems to identify and select for technical reviews, loans and lenders within each homeownership center's jurisdiction that pose a high insurance risk to HUD	Open, pending full implementation expected Fall 2001	GAO - Stan Ritchick 512-6788 HUD - Vance Morris 708-2121 x2204

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RCED-00-117			
Single-Family Housing: Measures Needed to Encourage Better Performance by Management and Marketing Contractors (05/12/00)	to develop more effective methods, such as specific incentives or penalties, to encourage contractors to reduce the number of properties that are in the inventory longer than 6 months	Open, pending HUD addressing the aged inventory problem	GAO - Stan Ritchick 512-6788 HUD - Joe McCloskey 708-1672 x2296
RCED-98-117			
Housing Finance: FHA's Risk Sharing Programs Offer Alternatives for Financing Affordable Multifamily Housing (04/23/98)	take steps to correct current flaws in the information systems supporting the programs	Open, pending implementation expected December 2001	GAO - Jim Vitarello 512-5119 HUD - Joe Malloy 708-3000 x2524
RCED-99-217			
Multi-Family Housing: HUD Missed Opportunities to Reduce Costs on Its Uninsured Section 8 Portfolio (07/30/99)	require HUD to enforce its regulation prohibiting dual fees unless there is a documented, sound and equitable basis for waiving the regulation....identify all Section 8 contracts for which state agencies receive both an administrative fee under the Section 8 contract and an override fee, including those contracts that are not subject to a refunding agreement with HUD	Open, pending implementation of proposed retroactive waiver process	GAO - Rose Schuville 312 220-7718 HUD - Jim Mitchell 708-3944 x2612
RCED-99-72			
Single-Family Housing: Weaknesses in HUD's Oversight of the FHA Appraisal Process (04/16/99)	determine the department's authority to hold FHA-approved lenders accountable for poor-quality FHA appraisals performed by the appraisers they select from FHA's roster and issue policy guidance that sets forth the specific circumstances under which and actions by which HUD may exercise this authority	Open, pending our review of recent HUD activity	GAO - Stan Ritchick 512-6788 HUD - Vance Morris 708-2121 x2204

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RCED-98-174			
Public Housing Subsidies: Revisions to HUD's Performance Funding System Could Improve Adequacy of Funding (06/19/98)	consider establishing a process that (1) allows housing agencies to appeal their expense levels when they believe that significant changes have occurred over time in their operating circumstances that cause their subsidy to be inappropriate and (2) HUD can use to review housing agencies' expense levels that it believes may be excessive	Open, pending results of Harvard University study	GAO - Don Watson 214 777-5609 HUD - Steven Sprague or Regina Gill 708-1872
RCED-99-210			
Public Housing: HUD Has Several Opportunities to Promote Private Management (07/26/99)	(1) encourage housing authorities through their planning process to consider and adopt asset management principles, including project-based budgeting and accounting; (2) encourage small housing authorities to look for opportunities to achieve efficiencies by forming consortia or joint ventures that could include third parties; and (3) provide incentives for housing authorities to make more cost-effective use of their resources	Open, (third part only, pending the outcome of the Harvard University study)	GAO - Andy Finkel 512-6765 HUD - Bill Minning 708-0713 x4115
RCED-00-168			
HUD Housing Portfolios: HUD has Strengthened Physical Inspections but Needs to Resolve Concerns About Their Reliability (07/25/00)	revise REAC's April 2000 quality assurance plan as necessary to ensure the quality assurance activities it contains will provide REAC with the information it needs to evaluate four key areas....reevaluate whether the plan contains appropriate criteria for quality assurance personnel to use in assessing each of the activities covered by the plan	Open, pending additional action from HUD	GAO - Rick Hale 512-3090 HUD - William Hill 708-4932 x3279
	periodically issue reports describing the quality assurance activities that it has performed and the results of these activities	Open, pending additional action from HUD	GAO - Rick Hale 512-3090 HUD - William Hill 708-4932 x3279

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HEHS-00-119			
Benefit and Loan Programs: Improved Data Sharing Could Enhance Program Integrity (09/13/00)	develop a strategy for obtaining access to automated data from financial institutions, determine the most cost-effective, efficient method for obtaining such data, and report to the Congress on any legislation that would be needed to implement this strategy....coordinate with SSA and OCSE to determine what strategies are the most effective for obtaining this information	Open, pending HUD action	GAO - Sigurd Nilsen 512-7003 HUD - Gloria Cousar 708-0950
GAO-01-460			
Mortgage Financing: FHA's Fund Has Grown, but Options for Drawing on the Fund Have Uncertain Outcomes (02/28/01)	develop criteria for measuring the actuarial soundness of the Mutual Mortgage Insurance Fund....criteria should specify the economic conditions that the Fund would be expected to withstand and may specify capital ratios currently consistent with these criteria	Open (new)	GAO - Matt Scire 512-6794 HUD - Judy May 401-0450 x3239
	give more attention to tests of the Fund's ability to withstand appropriate stresses....including more severe scenarios that capture worse-than-expected loan performance that may be due to economic conditions and other factors, such as changes in policy and the conventional mortgage market	Open (new)	GAO - Matt Scire 512-6794 HUD - Judy May 401-0450 x3239
	develop better tools for assessing the impact these changes may have on the volume and riskiness of loans that FHA insures....such changes should be made in small increments so that their impact can be monitored and adjustments can be made over time	Open (new)	GAO - Matt Scire 512-6794 HUD - Judy May 401-0450 x3239

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GAO-01-663T			
Housing and Urban Development: Comments of HUD's Fiscal Year 2002 Budget Request (04/25/01)	develop systems that routinely provide timely, reliable information on the status of unexpended funds for the purpose of quantifying the amount available for recapture or rescission; routinely incorporate this information into the management and operations of programs; and consistently use this information in formulating its budget request, clearly demonstrating how it is taking these balances into account when setting forth its budget needs	Open (new)	GAO - Carol Anderson-Guthrie 214 777-5739 HUD - Ronald Spraker 708-2865 x6851

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