

January 2001

# Major Management Challenges and Program Risks

Department of Housing and  
Urban Development





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January 2001

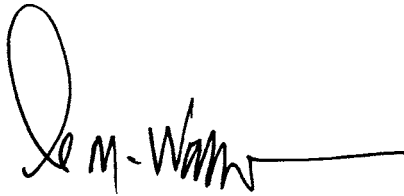
The President of the Senate  
The Speaker of the House of Representatives

This report addresses the major performance and accountability challenges facing the Department of Housing and Urban Development (HUD) as it seeks to encourage homeownership, promote affordable housing, and revitalize communities. It includes a summary of actions that HUD has taken and are under way to address these challenges. It also outlines further actions that GAO believes are needed. This analysis should help the new Congress and administration carry out their responsibilities and improve government for the benefit of the American people. This report is part of a special series, first issued in January 1999, entitled the *Performance and Accountability Series: Major Management Challenges and Program Risks*. In that series, GAO advised the Congress that it planned to reassess the methodologies and criteria used to determine which federal government operations and functions should be highlighted and which should be designated as “high risk.” GAO completed the assessment, considered comments provided on a publicly available exposure draft, and published its guidance document, *Determining Performance and Accountability Challenges and High Risks* (GAO-01-159SP), in November 2000.

This 2001 *Performance and Accountability Series* contains separate reports on 21 agencies—covering each cabinet department, most major independent agencies, and the U.S. Postal Service. The series also includes a governmentwide perspective on performance and management challenges across the federal government. As a companion volume to this series, GAO

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is issuing an update on those government operations and programs that its work identified as “high risk” because of either their greater vulnerabilities to waste, fraud, abuse, and mismanagement or major challenges associated with their economy, efficiency, or effectiveness.

A handwritten signature in black ink, appearing to read "D. M. Walker", with a long horizontal line extending to the right.

David M. Walker  
Comptroller General  
of the United States

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# Overview

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The Department of Housing and Urban Development (HUD) encourages homeownership by providing mortgage insurance through its Federal Housing Administration (FHA) for about 7 million homeowners who otherwise might not have qualified for loans, as well as by managing about \$508 billion in insured mortgages and \$570 billion in guarantees of mortgage-backed securities. It also makes housing affordable for about 4 million low-income households by insuring loans for multifamily rental housing and providing rental assistance. In addition, it has helped to revitalize over 4,000 localities through community development programs. To accomplish these missions, HUD relies on the performance and integrity of thousands of mortgage lenders, contractors, property owners, public housing agencies, communities, and others to administer its programs. Strong oversight and management are critical to ensure that HUD's reliance on these third parties results in the effective and efficient stewardship of federal funds and the accomplishment of federal programs' goals and objectives.

In the late 1980s, various management deficiencies led to a number of widely publicized instances of waste, fraud, abuse, and mismanagement at HUD. In 1994, we designated all of HUD's major program areas as high risk because four major departmentwide deficiencies continued to undermine the integrity and accountability of HUD's programs. These deficiencies included (1) internal control weaknesses, such as a lack of necessary data and management processes; (2) poorly integrated, ineffective, and generally unreliable information and financial management systems; (3) organizational deficiencies, such as overlapping and ill-defined responsibilities and authorities between HUD headquarters and field organizations, and a fundamental lack of management accountability and responsibility; and (4) an insufficient mix of staff with the proper skills.



In 1997, HUD initiated its 2020 Management Reform Plan to address these and other deficiencies. In our January 1999 report on HUD's management challenges and program risks and our high-risk series update,<sup>1</sup> we reported that HUD had made credible progress in overhauling its operations but that several reforms were in the early stages of implementation. Accordingly, we concluded that HUD's management deficiencies, taken together, continued to place the integrity and accountability of the Department's programs at high risk.

During the past 2 years, HUD has continued to make progress in addressing these problems. To address its internal control weaknesses, HUD has since January 1999 implemented new early warning monitoring tools, including the first physical inspections and financial assessments of the entire multifamily housing inventory. Through a large-scale computer matching initiative, which linked income data reported by tenants for housing and tax purposes, HUD also identified and sent letters to 211,000 households that may have underreported their incomes for housing purposes, thereby resulting in excess subsidy payments, estimated by HUD at \$3.1 billion over the last 4 years.

To improve its information and financial management systems, HUD has taken actions to develop an information technology investment management process to improve and strengthen the selection, control, and evaluation of information technology projects. In addition, HUD has reduced the number of financial management systems that are not in compliance with federal requirements.

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<sup>1</sup>Major Management Challenges and Program Risks: Department of Housing and Urban Development (GAO/OCG-99-8, Jan. 1999 and High-Risk Series: An Update (GAO/HR-99-1, Jan. 1999).

To strengthen organizational links between headquarters and the field, improve accountability, and accomplish its missions more efficiently, during fiscal year 1999 HUD substantially completed its reorganization under the 2020 Management Reform Plan. Staff and workload were transferred from the field to several new specialty centers, which are now operating and have started to produce some results. For example, the Homeownership Centers reduced the average time for processing single-family mortgage loans from 4 to 6 weeks to 2 to 3 days and the Enforcement Center relocated 427 families from substandard housing and recovered \$12.6 million from property owners for ineligible costs.

To ensure that it has the appropriate mix of staff with the proper skills to carry out its missions, HUD piloted a new resource estimation and allocation process to determine appropriate staffing levels. It also provided more training and travel funds for its staff.

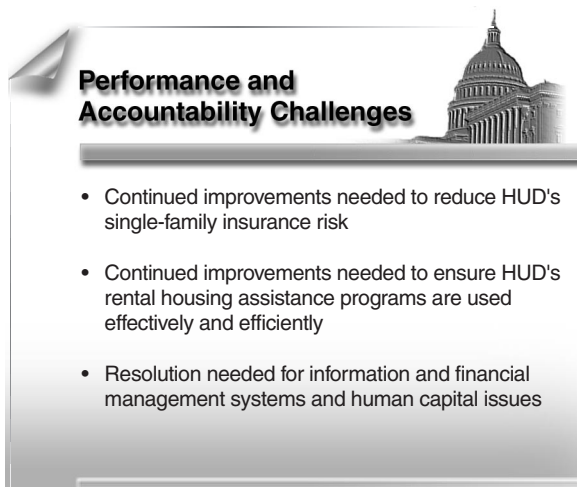
HUD has taken important steps toward addressing some of its other management deficiencies. Its top management has given high priority to implementing the Department's 2020 Management Reform Plan, the Department's reorganization is substantially complete, and the Department's reform efforts have resulted in some improvements. Recognizing the progress HUD has made and consistent with our criteria for determining high risk,<sup>2</sup> we are redefining and reducing the number of HUD programs deemed to be high-risk. Specifically, because of the actions taken by HUD in response to our recommendations to improve its management controls over its Community Planning and Development programs, we no longer believe this HUD program area is at high risk. However, significant weaknesses (i.e.,

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<sup>2</sup>*Determining Performance and Accountability Challenges and High Risk* (GAO-01-159SP, Nov. 2000).

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internal controls, information and financial management systems, organizational deficiencies, and staffing problems) still persist in two of HUD's major program areas which remain at high-risk—single-family mortgage insurance and rental housing assistance. In addition, HUD needs to continue addressing management challenges in two other areas—information and financial management systems and human capital.

A graphic titled "Performance and Accountability Challenges" featuring a stylized illustration of the U.S. Capitol building in the background. The title is in bold black text. Below the title is a list of three bullet points.

**Performance and Accountability Challenges**

- Continued improvements needed to reduce HUD's single-family insurance risk
- Continued improvements needed to ensure HUD's rental housing assistance programs are used effectively and efficiently
- Resolution needed for information and financial management systems and human capital issues

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### Single-Family Mortgage Insurance Programs

To reduce financial risks, HUD's FHA needs to continue to improve its management over home mortgage loans made by private lenders that it insures against nearly all losses. While various factors, including a strong economy, have resulted in the accumulation of capital reserves of about \$16.6 billion on FHA-insured home loans valued at about \$454 billion, we estimate that FHA lost about \$1.9 billion during fiscal year 2000 on the sale of foreclosed homes that it had insured. We and HUD's Inspector General have identified opportunities to strengthen FHA's single-family mortgage insurance

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programs' management and internal controls and reduce financial risks. These include:

- strengthening the integrity of the single-family loan origination process;
- promoting better monitoring of lenders, appraisers, and property management and marketing contractors; and
- ensuring that sufficient staff are available and have the skills needed to carry out FHA's home loan mission.

HUD also needs to resolve two material internal control weaknesses identified by its Inspector General relating to FHA's information and financial management systems—(1) fully reconciling accounting and budget systems for loan guarantees to ensure that all credit subsidy amounts are recorded properly and (2) improving information systems to support business processes more effectively.

The Department has begun to address many of our recommendations and those of the Inspector General, but it has not completed actions to implement most of them. Because of the programs' size, the variety of management challenges FHA faces, and the potential liability FHA has assumed, these programs remain at high-risk. To reduce the programs' financial risks, FHA must continue its efforts to strengthen its controls and monitoring. This includes completing actions on our recommendations, such as clarifying HUD's authority to hold FHA-approved lenders accountable for poor-quality FHA single-family appraisals. HUD must also continue its efforts to resolve the programs' two material internal control weaknesses and assess its staffing needs.

HUD. However, HUD is able to serve fewer than half of the households who are eligible for assisted housing. Consequently, it is essential that HUD ensure that these programs are used efficiently and effectively to maximize the number of households it can assist. While the Department has made improvements, there are still significant opportunities to (1) reduce excess subsidy payments which have totaled about \$3.1 billion over the last 4 years by ensuring that only eligible families occupy housing units and that those families are paying the correct rents; (2) ensure that providers of rental housing maintain housing that is decent, safe, sanitary, and in good condition; and (3) be certain that HUD has the capital resources and controls it needs to detect and address problems that exist in its rental housing assistance programs.

HUD is addressing these challenges as well as our recommendations and those of the Inspector General. However, its actions are not yet complete. Because of their size and complexity and the opportunity to provide assisted housing to more low-income households through better management, these programs remain at high-risk. HUD must continue to strengthen its internal controls by completing its efforts to ensure that correct rental housing subsidies are paid. It must also complete actions on our recommendations aimed at improving the quality of contractors' physical inspections of the condition of public and multifamily housing. This includes revising its quality assurance activities to ensure that they provide the timely, reliable, and useful information needed for HUD to assess, among other things, compliance with inspection contracts.

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Information and  
Financial  
Management Systems  
and Human Capital  
Issues

To become a high-performing organization, HUD needs to resolve management challenges related to information and financial management systems and human capital. HUD has a variety of actions under way to address its information and financial management systems and human capital challenges.

HUD has determined that its financial management systems, largely deployed under its Financial Systems Integration effort, do not meet all of its needs. HUD announced its intention to replace these systems, and a new plan is in the early stages of development. It is too soon to tell whether HUD will be successful in this latest attempt to deploy an integrated financial management system to upgrade the Department's program and financial management capacity. It is also too soon to assess the effectiveness of actions HUD has taken to address delays in the preparation of its consolidated financial statements. After issuing an unqualified opinion on HUD's fiscal year 1998 consolidated financial statements, the Inspector General was unable to issue an opinion the following year. This occurred because, as the Inspector General reported in March 2000, HUD had experienced problems implementing a new general ledger system and could not prepare its fiscal year 1999 consolidated financial statements in time for the Inspector General to complete the audit by the statutory deadline. Whether HUD has resolved this problem will not be known until the fiscal year 2000 financial statements audit is completed in the spring of 2001. It is therefore critical that HUD, like most other federal agencies, continue to focus on improving its information technology management processes to help ensure success in these and other systems initiatives across the Department.

HUD must also resolve a number of human capital issues. First, it must make further adjustments to workload. About half of the workload remains to be

transferred to the Financial Management Center, the workload of two other centers is less than intended, and HUD must finish transferring functions from the field to the centers as planned. Second, it must complete its actions to develop departmental systems for measuring work including considering whether the benefits of the approximately 600 Community Builders it has hired in recent years are worth the costs of hiring and training them. Lastly, it must staff its programs adequately. In responding to a recent survey, HUD managers at the centers and in the field told us they did not have enough staff. Field managers noted, for example, that although some of their former functions were shifted to the centers, other functions have not yet been transferred as planned, and new programs, regulations, and management initiatives have increased their responsibilities without increasing their staff.

To resolve these management challenges and more effectively manage its programs, HUD needs to (1) deploy a reliable financial management system that meets its program and financial management needs and complies with federal requirements, (2) continue to develop a process to identify and justify its staff resource requirements, and (3) ensure that staff are available and have the skills needed to carry out the work assigned. HUD's human capital problems can be seen as part of a broader pattern of human capital shortcomings that have eroded mission capabilities across the federal government. (See *High-Risk Series: An Update* (GAO-01-263, Jan. 2001) for a discussion of human capital as a newly designated governmentwide high-risk area.)

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# Major Performance and Accountability Challenges

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HUD has wide-ranging responsibilities—from increasing homeownership to providing affordable rental housing to spurring economic development. HUD meets these responsibilities generally by relying on the performance and integrity of thousands of diverse entities that administer its programs, making effective oversight and adequate information systems crucial to the achievement of its objectives. In fiscal year 1999 alone, about 10,000 lending institutions, in total, made 1.3 million FHA-insured single-family mortgages valued at about \$125 billion. Management and marketing contractors manage FHA's inventory of about 50,000 single-family homes at a 5-year cost to HUD of about \$927 million. About 4,500 housing authorities administer HUD's public housing and tenant-based rental assistance programs, which serve over 2.8 million households. Section 8 contract administrators<sup>1</sup> will be managing over half of HUD's 22,000 project-based Section 8 contracts covering about 993,000 multifamily housing units.

Over the years, we, HUD's Inspector General, and others have documented problems with HUD's performance and management and have recommended reforms. This report summarizes our recent findings and those of others on HUD's efforts to (1) make mortgage financing more accessible to homebuyers; (2) provide decent, affordable rental housing; and (3) address other management challenges that cut across HUD's programs.

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<sup>1</sup>HUD contracts with private property owners to provide housing rental assistance, called Section 8 project-based assistance, on behalf of eligible low-income households. In the past, HUD field staff managed most housing assistance contracts.



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Continued  
Improvements  
Needed to Reduce  
HUD's Single-  
Family Insurance  
Risk

FHA administers several programs aimed at making mortgage financing more accessible to homebuyers, particularly low-income and first-time homebuyers. To expand homeownership, FHA insures private lenders against nearly all losses on mortgages that finance single-family homes. As of the end of fiscal year 1999, FHA had insurance commitments on about 6.7 million mortgages with a value of about \$454 billion. In recent years, various factors, especially favorable economic conditions, have resulted in the accumulation of capital reserves of about \$16.6 billion and a national homeownership rate that has increased to an all-time high.

FHA's single-family mortgage insurance programs have undergone significant changes since HUD initiated its 2020 Management Reform Plan. Specifically, HUD consolidated its single-family operations (previously carried out in 81 field offices) into four Homeownership Centers, reduced its staffing in these operations by about 50 percent, began privatizing or contracting for most property disposition activities, and eliminated most loan-servicing functions by selling much of its inventory of HUD-held mortgages. Through these reforms, HUD expected to significantly reduce its staffing, cut insurance endorsement processing time, improve underwriting and loss mitigation,<sup>2</sup> and make more single-family loans to targeted populations. HUD also expected the reforms to address problems such as poor control and monitoring of its single-family properties and inconsistent delivery of services.

Our reviews since January 1999 indicate that HUD and FHA have made considerable progress in streamlining

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<sup>2</sup>FHA's loss mitigation program seeks, among other things, to mitigate losses resulting from foreclosure by using alternatives to foreclosure, such as loan modifications.

operations and making FHA's single-family mortgage insurance programs more efficient. However, we estimate that FHA continues to lose funds (about \$1.9 billion during fiscal year 2000) on the sale of foreclosed homes that it had insured. Our reviews and those of the Inspector General also show that significant deficiencies remain in FHA's internal controls, human capital strategies, and information and financial management systems. Because of these deficiencies, the single-family mortgage insurance programs remain at high risk.

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**Internal Control  
Weaknesses Exist in  
Single-Family  
Operations**

Since 1999, we have identified a number of internal control weaknesses in the management and monitoring of FHA's single-family insurance programs in the areas of loan origination, appraisals, and property disposition. In response to our recommendations and those of the Inspector General, FHA has initiated actions to address these issues. However, most of these corrective actions have not yet been completed, and some were taken too recently to determine whether they will ultimately resolve the internal control weaknesses.

- In April 2000, we reported that HUD's process for granting FHA lenders direct authority to endorse FHA-insured home loans provides limited assurance that lenders receiving this authority are qualified.<sup>3</sup> We also noted that HUD's monitoring of lenders does not adequately focus on the lenders and loans that pose the greatest insurance risk to the Department. We made several recommendations to improve HUD's processes for approving lenders to underwrite mortgages, target lenders and loans for quality control reviews, and take enforcement actions against poorly performing lenders.

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<sup>3</sup>*Single-Family Housing: Stronger Oversight of FHA Lenders Could Reduce HUD's Insurance Risk* (GAO/RCED-00-112, Apr. 28, 2000).

According to HUD, it began addressing some of these recommendations in late 2000 and will implement other actions in 2001. In addition, HUD reported that the Enforcement Center and Credit Watch and Neighborhood Watch programs have helped improve its monitoring of lenders.<sup>4</sup> HUD also reported that such increased monitoring resulted in referrals of more lenders to its Mortgagee Review Board,<sup>5</sup> which sanctioned 61 lenders in fiscal year 2000, up from 18 in fiscal year 1997. Fifty of these lenders were fined a total of \$3.3 million.

- In April 1999, we reported that HUD was not adequately monitoring the performance of appraisers or holding appraisers accountable for the quality of their appraisals of single-family properties to be insured by FHA.<sup>6</sup> When incomplete or inaccurate appraisals result in overvaluations of property, FHA may be exposed to greater financial risks. Three of HUD's four Homeownership Centers were not meeting a requirement to conduct on-site evaluations of completed appraisals for not fewer than 10 percent of the appraisals in their jurisdictions, and HUD did not field-review the work of thousands of appraisers who conducted 10 or more FHA appraisals. We also found that few poorly performing appraisers were sanctioned. Officials at two Homeownership Centers attributed some of these problems to a lack of staff, a lack of adequate travel funds, and gaps in documentation that occurred

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<sup>4</sup>Credit Watch and Neighborhood Watch are two programs that enable FHA to analyze trends in claim and default data by lender and impose sanctions on problem lenders.

<sup>5</sup>The Mortgagee Review Board is the entity within HUD that can impose administrative sanctions against a lender, withdraw a lender's authority to make FHA-insured loans, or both.

<sup>6</sup>*Single-Family Housing: Weaknesses in HUD's Oversight of the FHA Appraisal Process* (GAO/RCED-99-72, Apr. 16, 1999).

during the consolidation of single-family mortgage insurance activities.

Additionally, HUD has not aggressively enforced its policy to hold lenders equally accountable with the appraisers they select for the accuracy and thoroughness of appraisals. We reported that this problem occurred because the staff for HUD's Mortgage Review Board did not believe that HUD had the authority to hold a lender accountable for the quality of an appraisal simply because the lender had selected the appraiser. Although HUD has begun implementing many of our recommendations to improve appraisals and has a policy to hold lenders responsible for the quality of appraisals, it has not yet clarified the circumstances under which and the actions by which the policy should be enforced.

- In May 2000, we reported that most of the contractors hired by HUD to manage and market the single-family homes it had acquired following foreclosures were having difficulty maintaining and securing the properties.<sup>7</sup> During fiscal year 1999, HUD awarded contracts for managing and marketing these single-family properties. The contractors increased the net recovery from sales (the percentage of a property's value that HUD realizes after paying all costs associated with managing the property) from 79.7 to 80.2 percent, as well as the number of properties sold.

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<sup>7</sup>*Single-Family Housing: Stronger Measures Needed to Encourage Better Performance by Management and Marketing Contractors* (GAO/RCED-00-117, May 12, 2000).

However, we found that the contractors were having problems meeting their performance requirements and stronger measures were needed to encourage better performance by the contractors. During our visits to properties, we found evidence of vandalism, disrepair, or inadequate security. A public accounting firm also identified weaknesses in FHA's monitoring and management of its single-family property inventory, which resulted in an internal control deficiency in FHA's fiscal year 1999 financial statements audit. Problems in maintaining single-family properties have existed for some time. We found similar problems with HUD's oversight of contractors during a similar review in 1998, when we reviewed the contractors maintaining HUD's single-family properties at that time.<sup>8</sup>

According to HUD, it (1) has begun to implement measures to ensure that the new management and marketing contractors are correcting problems in a timely manner and (2) is negotiating contract modifications that permit monetary penalties for poor maintenance and rewards for excellent maintenance, as suggested by the Inspector General and others.

- In June 1999, we reported that HUD had done little to address the management problems identified by the Inspector General and others in its 203(k) program, which provides loans for home rehabilitation.<sup>9</sup> We reported that these problems include concerns that the design of this program encourages risky property deals and overstates property appraisals and that homes are not being properly rehabilitated. We also reported HUD was not ensuring that lenders comply with the program's guidelines or that home

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<sup>8</sup>*Single Family Housing: Improvements Needed in HUD's Oversight of Property Management Contractors* (GAO/RCED-98-65, Mar. 27, 1998).

<sup>9</sup>*Homeownership: Problems Persist with HUD's 203(k) Home Rehabilitation Loan Program* (GAO/RCED-99-124, June 14, 1999).

inspectors and consultants are properly trained and monitored. The claims rate for loans endorsed from fiscal year 1994 through fiscal year 1996 was double that for loans made under the other HUD single-family programs.

According to HUD, the 203(k) program represents a very small percentage of its single-family loans, and the Department has recently taken steps to improve the program. Specifically, as of July 2000, HUD made mortgagees fully responsible for ensuring that inspections of rehabilitated homes are completed and for approving payments to contractors. Furthermore, consultants who are responsible for designing and overseeing home rehabilitation loans have been required to register with HUD since September 26, 2000, in order to continue participating in the program.

Internal control weaknesses in FHA's single-family mortgage insurance programs have also, at times, led to fraud, waste, and abuse. In its latest semiannual report, HUD's Office of Inspector General stated that its work demonstrates a need for tighter internal controls in FHA's single-family mortgage insurance programs. Among other things, the Inspector General noted that (1) 39 individuals involved in a \$110 million fraudulent loan scheme were indicted in a case involving property "flipping" (single-family properties that are bought and quickly resold at inflated prices based on fraudulent appraisal values) and (2) the use of fraudulent documentation to qualify borrowers for FHA-insured mortgages led to criminal indictments and convictions in several communities.

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**Human Capital Issues  
Remain**

Both we and the Inspector General have found that human capital issues remain a concern for HUD in its single-family mortgage insurance programs. Staffing for the single-family programs was reduced by about 50

percent after HUD implemented the 2020 Management Reform Plan and consolidated the single-family workload into the four Homeownership Centers. A lack of staff and insufficient training and travel resources were cited as reasons for some of the problems we identified in our reviews. Human capital issues also surfaced in reviews performed by the Inspector General and in the responses of HUD managers to a survey we recently conducted. Nevertheless, HUD reports substantial increases in productivity in some areas as a result of the consolidations. For example, the processing time for FHA single-family loan endorsements has declined from 4 to 6 weeks to 2 to 3 days, even though HUD reported a record 1.3 million loans were endorsed in fiscal year 1999.

Between September and October 2000, we surveyed HUD managers to obtain their views on staffing and workload issues after HUD implemented its 2020 Management Reform Plan. This survey was similar to one we conducted in 1996, before HUD implemented its 2020 plan. In responding to our 2000 survey, about half the single-family managers reported that they had fewer staff than necessary and their workload had continued to increase. About 53 percent of the single-family managers surveyed said they had fewer staff than necessary to carry out the activities in their area of responsibility, and about 58 percent said their workload had increased over the last 2 years. In 1996, 61 percent of the single-family managers we surveyed said they had fewer staff than necessary, and 50 percent said their workload had increased.

On the other hand, most single-family managers said they were satisfied with the skills of their employees and recognized that those skills had improved greatly in recent years. About 89 percent of the single-family managers said they were satisfied with the current match between the skills of their staff and the skills these staff needed to carry out their duties, and about 53

percent said the skills of their staff had improved greatly over the past 2 years. However, about 79 percent advocated more training in technical skills related to job responsibilities, and about 74 percent said training for using information systems should be increased. These results are consistent with those of our 1996 survey, although the percentage of managers who (1) were greatly satisfied with skills of their staff and (2) said that these skills had improved greatly over the past 2 years was much higher than in 1996.

The following examples illustrate human capital issues we identified in our reports on FHA's single-family mortgage insurance programs:

- In our April 2000 report on HUD's oversight of FHA lenders, Homeownership Center officials stated that high-risk lenders were not always reviewed, in part because of inexperienced staff. The officials explained that many of the staff assigned to review lenders came from a pool of unassigned staff after the reorganization and had no background in lender-monitoring and credit issues. To address this problem, the officials said they provided both classroom and on-the-job training to the new staff.
- In our June 1999 report on the 203(k) mortgage insurance program, we reported that HUD has not committed the resources needed to adequately oversee the program. We reported that officials at two Homeownership Centers told us they do not have staff qualified to do quality assurance reviews for 203(k) home rehabilitation loans. Quality assurance reviews are important because the 203(k) program involves multiple entities and cost estimates, including a HUD-approved consultant to determine the extent of work needed and cost estimates for this work and an inspector to monitor the progress of rehabilitation work. In addition, according to one official responsible for 17 states, the center did not have sufficient travel funds to



provide adequate oversight of any of its single-family programs, including the 203(k) program, during the first quarter of fiscal year 1999.

- In our April 1999 report on HUD's oversight of appraisers, officials at the Philadelphia and Denver Homeownership Centers told us that they rarely conducted evaluations of field review contractors because they lacked sufficient staff and travel resources.<sup>10</sup> They neither tracked the percentage of each contractor's work that received field reviews nor evaluated the contractor's performance. As a result, HUD's ability to assess the quality of the appraisals used to support FHA loans was weakened.

HUD's Office of Inspector General has also expressed concerns about the adequacy of FHA's resources in its reports on HUD's and FHA's financial statements.<sup>11</sup> Until February 2000, the Inspector General reported internal control weaknesses related to FHA's staff and administrative resources as a material internal control weakness. The report on FHA's fiscal year 1999 financial statements audit no longer reported these problems as a separate material weakness. Instead, the Inspector

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<sup>10</sup>HUD contracts with licensed appraisers to conduct field reviews of completed appraisals. About three-quarters of the 80,958 field reviews conducted in fiscal year 1998 were performed by field review contractors.

<sup>11</sup>HUD's Inspector General contracts with independent public accountants to audit the financial statements of HUD's FHA. The Inspector General's report on HUD's consolidated financial statement audit includes the material internal control weaknesses identified by the independent public accountants at FHA, as well as the material weaknesses identified by the Inspector General at HUD. Because the Inspector General is responsible for the FHA audit and reports on both FHA's and HUD's material weaknesses, this report refers to both sets of material weaknesses as material weaknesses identified by the Inspector General in its audits of HUD. See *U.S. Department of Housing and Urban Development Attempt to Audit the Fiscal Year 1999 Financial Statements*, Office of Inspector General (00-FO-177-0003, Mar. 1, 2000) and *Federal Housing Administration, Audit of the Fiscal Year 1999 Financial Statements*, Office of Inspector General (00-FO-131-0002, Feb. 29, 2000) (prepared by KPMG LLP for the Office of Inspector General).

General reassessed the problems in light of improvements HUD made in addressing its resource issues. The Inspector General recategorized the weakness as a cause contributing to other reportable conditions. However, the Inspector General noted that significant problems remain with HUD's resource issues and that it is critical for the Department to continue addressing the previously identified problems by completing ongoing plans.

Lastly, the National Academy of Public Administration (NAPA) also reported in October 1999, in a pilot test of a proposed resource estimation methodology, that staffing was insufficient for the processing and underwriting functions of the Office of Housing's single-family mortgage insurance program at both headquarters and the Denver Homeownership Center.<sup>12</sup> This pilot test led to HUD's initiating a resource estimation and allocation study departmentwide. The first phase began in August 2000, and the entire study is expected to be finished in about 18 months.

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**Information and  
Financial  
Management Systems  
Concerns**

Public accounting firms, in auditing FHA's financial statements, have since 1993 found that the statements were presented fairly, in all material respects, in conformity with generally accepted accounting principles. However, the auditors have cited material internal control weaknesses related to FHA's accounting and information systems. These weaknesses, according to the Inspector General's March 2000 report on HUD's financial statements, were that (1) FHA's budgetary and financial accounting controls must be improved and (2)

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<sup>12</sup>Aligning Resources and Priorities at HUD: Designing a Resource Management System, A Report by a Panel of the National Academy of Public Administration for Congress and the Department of Housing and Urban Development (Oct. 1999).

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FHA's information systems must be enhanced to more effectively support FHA's business processes.

In October 2000, we reported that HUD had actions under way or planned to address these weaknesses, including (1) fully reconciling accounting and budget systems for loan guarantees to ensure that all credit subsidy amounts are recorded properly and (2) continuing to modernize FHA's information and financial management systems and reduce the agency's reliance on older systems.<sup>13</sup> We concluded that FHA's actions should help it continue to make progress in resolving these and other material weaknesses. FHA has undertaken extensive efforts to improve its financial reporting and has developed plans to obtain a more current commercially available financial management system. (For more information, see our discussion in this report of HUD's information and financial management systems and human capital issues.)

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**Continued  
Improvements  
Needed to Ensure  
That HUD's Rental  
Housing Assistance  
Programs Are Used  
Effectively and  
Efficiently**

HUD encourages the development of affordable rental housing through a wide range of assistance and incentives. Specifically, it provides (1) mortgage insurance through FHA for the construction and rehabilitation of multifamily developments, (2) project-based rental assistance to owners of insured and uninsured projects, (3) grants for the development of multifamily housing, (4) operating subsidies for public

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<sup>13</sup>*HUD Management: Status of Actions to Resolve Serious Internal Control Weaknesses* (GAO-01-103, Oct. 16, 2000).

housing agencies, and (5) tenant-based vouchers for eligible households to use in securing privately owned housing.

HUD's rental assistance programs are administered by about 4,500 housing authorities, as well as under contracts covering about 22,000 privately owned properties. The assistance provided under these contracts is called Section 8 project-based assistance. HUD, often working through third parties, is responsible for ensuring that the properties remain in good physical and financial condition and that the households receiving rental assistance meet eligibility requirements and obtain the proper amount of assistance.

In fiscal year 1999, HUD provided about \$19 billion in rental subsidies to make housing affordable for an estimated 4 million households. Under HUD's Section 8 programs, about 1.4 million households received tenant-based vouchers and 1.3 million households received project-based housing for which HUD contracted directly with housing providers. HUD also provided funds for 1.2 million units of public housing and, through FHA, insured about 15,450 multifamily mortgages with an unpaid principal balance of nearly \$53 billion as of the end of fiscal year 1999.

Despite the magnitude of the assistance it provides, HUD is able to serve fewer than half of those who are eligible for assisted housing. In its current strategic plan, HUD reports that in 1997, a record 5.4 million households experienced worst-case housing needs, including 2 million families with children and 1.2 million elderly households.<sup>14</sup> At the same time, about 7 percent of all households and 15 percent of very-low-income renters lived in housing with severe or moderate physical problems.

HUD faces considerable challenges in closing the gap between the number of households needing housing assistance and those that presently receive it. Furthermore, the fact that this gap exists places increased importance on HUD having internal controls that ensure that (1) existing housing subsidies are received only by eligible households and households receive no more than the amounts to which they are entitled and (2) housing providers receiving rental assistance payments from HUD comply with HUD's standards for housing that is decent, safe, sanitary, and in good repair. Our reviews and those of the Inspector General show that significant deficiencies remain in these areas as well as in human capital strategies. Because of these deficiencies, the rental housing assistance programs remain at high risk of fraud, waste, abuse, and mismanagement.

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**Actions to Improve  
Internal Controls  
Over Rental Housing  
Subsidies Need to Be  
Completed**

HUD estimates that it paid about \$935 million in excess subsidies in its rental assistance programs in fiscal year 1999. Moreover, HUD estimates that the percentage of excess subsidies it paid has increased in recent years. This overpayment occurred because tenants

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<sup>14</sup>Worst-case housing needs are defined as the needs of unassisted very-low-income renters who pay more than half of their income for housing or live in severely substandard housing.

**Major Performance and  
Accountability Challenges**

underreported or failed to report their income. In audits of HUD's consolidated financial statements, HUD's Inspector General has since fiscal year 1995 reported as a material internal control weakness that HUD needs to improve its efforts to ensure that it is paying correct rental subsidies.

To address this issue, HUD undertook a large-scale computerized comparison of the income data that tenants reported to housing authorities or property owners and to the Internal Revenue Service (IRS) or the Social Security Administration (SSA). This effort was designed to identify households that underreported their income to housing authorities or property owners. Underreporting is a problem for HUD because it increases the government's subsidy payments, reduces the number of families who may be assisted, and may result in ineligible families' retaining subsidized units. Table 1 presents the amount of assistance and excess rental subsidy paid for fiscal years 1996 through 1999.

**Table 1: Estimated Excess Subsidy Payments, Fiscal Years 1996-99**

<b>Fiscal year reported<sup>a</sup></b>	<b>Estimated excess subsidy payments</b>	<b>Program expenditures</b>	<b>Percentage of excess subsidies</b>
1996	\$538 <sup>b</sup>	\$19,257	2.8%
1997	804	18,069	4.4%
1998	857	18,600	4.6%
1999	935 <sup>c</sup>	18,606	5.0%

<sup>a</sup>The estimated excess subsidy payments are reported in footnotes to HUD's annual financial statements for HUD fiscal years ending September 30 of each year; however, the estimates are computed from data for the preceding calendar year.

<sup>b</sup>HUD's Inspector General concluded, in the audit of HUD's fiscal year 1996 financial statements (97-FO-177-0003), that HUD's \$538 million estimate of excess subsidies was understated because HUD did not include Supplemental Security Income in the computer matching. In addition, the Inspector General expressed concern about the completeness of HUD's tenant databases. HUD reported to us that

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## Major Performance and Accountability Challenges

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subsequent analysis shows that underreported SSI income has a nominal effect on the estimate of excess subsidies.

<sup>c</sup>Although HUD's Inspector General disclaimed on opinion on HUD's fiscal year 1999 financial statements (00-FO-177-0003), the reasons for the disclaimer did not relate to HUD's estimate of its excess subsidy payments.

HUD's Real Estate Assessment Center (REAC) assumed responsibility for the income-matching project and identified a potential universe of tenants whose income, as reported to IRS or SSA, exceeded the thresholds set by the computer-matching program. During the spring and fall of 2000, HUD sent letters to about 211,000 tenants who continued to reside in assisted housing, notifying them of possible discrepancies in the income data they had reported to the public housing agencies and IRS or SSA. Although the Department planned to send the letters out in October 1999, concerns raised by tenants and industry groups delayed the mailings until May 2000, and the mailing was not completed until October 2000. The delays in implementing this process mean that limited information is available to date on whether this effort will result in improved controls for ensuring that correct rental subsidies are paid for eligible tenants.

While this process is a significant step toward ensuring that correct rental subsidies are paid, there are problems in some of the data systems used for income matching. The income verification process used two HUD data sources for the tenant income information—the Multifamily Tenant Characteristics System for public housing residents and the Tenant Rental Assistance Certification System (TRACS) for Section 8 project-based renters. In a September 2000 report, the Inspector General stated that TRACS has data inaccuracies that decrease the effectiveness of HUD’s income verification efforts.<sup>15</sup> The Inspector General recommended that HUD ensure that planned actions to upgrade TRACS are followed through and that TRACS data are useful and cost-efficient. If these results are not possible, other alternatives should be pursued and TRACS discarded, according to the Inspector General.

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**Actions to Improve  
Internal Controls  
Over Housing Quality  
Need to Be  
Completed**

To address concerns about the quality of its subsidized housing and to ensure that it is subsidizing only decent housing, HUD contracted for physical and financial assessments of assisted and insured multifamily and public housing projects. During fiscal year 2000, HUD’s REAC oversaw physical inspections of HUD’s multifamily assisted housing and public housing inventory, conducted according to a standardized physical inspection process. As of April 2000, contractors had conducted baseline inspections for 26,528 multifamily properties and over 3,100 public housing authorities with 13,607 properties. These figures represent about 92 percent of the multifamily properties and all of the public housing properties that REAC intended to include in the baseline inspections. The results of the first physical inspections indicate that

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<sup>15</sup>*Housing Subsidy Payments Office of Housing, Office of Inspector General (00-KC-103-0002, Sept. 29, 2000).*



most properties are in satisfactory condition; however, concerns remain about the quality of those inspections.

In our July 2000 report on HUD's new physical inspection system,<sup>16</sup> we found that (1) when quality assurance staff performed on-site follow-up reviews to assess the adequacy of completed inspections, they found that the inspections were often not carried out consistently with REAC's requirements and (2) gaps exist in REAC's quality assurance procedures related to the inspections. Specifically, when the reviewers accompanied the contract inspectors to judge their performance, they found that 12 percent of 728 initial inspections did not meet REAC's standards. Furthermore, about 35 percent of another 819 inspections that received follow-up reviews did not meet the standards. We also accompanied REAC quality assurance reviewers on 10 follow-up reviews, and in each of the 10 reviews, the reviewer determined that the original inspection did not meet REAC's standards and required that a new inspection be performed.

Because these reviews were not performed randomly and the effects of the problems on the inspection scores cannot be readily determined, it is unclear to what extent problems with the inspections affected the overall inspection results. REAC officials acknowledged that the percentage of inspections identified as not meeting standards was unacceptable, although a precise tolerance level had not been established to evaluate the reliability of the inspections.

Our report noted that although REAC deserves credit for establishing quality assurance procedures, we found gaps or weaknesses in some of these procedures that

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<sup>16</sup>*HUD Housing Portfolios: HUD Has Strengthened Physical Inspections but Needs to Resolve Concerns About Their Reliability* (GAO/RCED-00-168, July 25, 2000).

substantially limited their effectiveness. For example, REAC did not have procedures for ensuring that quality assurance reviews were performed systematically or that the identified problems were resolved quickly and appropriately. Moreover, REAC did not always report the results of its quality assurance reviews to inspection contractors in a timely manner, and REAC did not have the systems and records needed to ensure that corrective actions were taken after problems were identified. While HUD has taken steps to address our recommendations concerning its quality assurance activities, it is too soon to determine whether these steps are sufficient to ensure the accuracy and reliability of REAC's physical inspection scores.

We also reported in July 2000 that despite the preponderance of satisfactory scores, a substantial number of properties were cited during the inspections for exigent (life-threatening) health and safety problems. For example, almost one-third of the multifamily and public housing properties received health and safety citations for defects that REAC categorizes as "life-threatening." Examples of such defects, according to REAC documents, include missing or inoperable smoke detectors, electrical system problems, hazards, missing fire extinguishers, and the presence of security bars. The properties were referred to field offices for immediate follow-up for urgent health and safety issues or to the Departmental Enforcement Center for enforcement action.

The purpose of HUD's Departmental Enforcement Center is to ensure that effective enforcement action occurs, including follow-up on the most serious violations found as a result of physical inspections of multifamily and public housing projects. The center, among other things, addresses problems of multifamily properties that have failed physical inspections or financial assessments or require corrective action by owners, lenders, and management agents who are not in

compliance with HUD's program guidance. As of September 30, 2000, the center had, among other things,

- relocated 427 families from substandard housing and identified nearly \$43 million in ineligible multifamily project costs and expenses and obtained \$12.6 million in recovery repayments,
- negotiated \$26.7 million in proposed owner investments to repair physical problems in multifamily properties, and
- secured another \$14.2 million from project replacement reserves to repair physical problems in multifamily properties.

Recently, in a December 2000 report on HUD-assisted housing, NAPA also reported on HUD's process for monitoring and overseeing assisted housing.<sup>17</sup> NAPA found that HUD is moving in a positive direction in improving the quality of HUD-assisted housing but that HUD's new quality assurance system has design deficiencies and barriers to effective implementation. Among its principal concerns, NAPA reported that (1) certain quality assurance elements were not well developed, particularly internal quality assurance procedures and the appeals process, and (2) many housing providers, including HUD, lack the necessary staffing, automated systems, and technical assistance and training capacity to effectively manage and implement the Department's quality assurance system. The report recommended that HUD modify its evolving quality assurance system significantly, make certain urgent operational improvements in the system that is now being used, and continue to refine the system to achieve greater flexibility and results. Specifically, NAPA's recommendations included

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<sup>17</sup>*Evaluating Methods for Monitoring and Improving HUD-Assisted Housing Programs*, National Academy of Public Administration (Dec. 2000).

- finalizing and implementing the appeals process for public housing agencies;
- enhancing HUD's capacity to administer the system, including improving telephone and electronic communications between housing providers and HUD's REAC and program offices; and
- upgrading the capacity of housing providers with new training opportunities and improved computer capacity.

Finally, in a November 2000 report on the performance of the public housing program,<sup>18</sup> we noted that for HUD to be held accountable for the performance of the public housing program, it must first hold housing agencies accountable for providing safe and decent housing and protecting the federal investment in their properties. HUD provides assistance to public housing agencies, spending nearly \$7 billion annually to develop affordable housing for low-income households. We reported that HUD needed to better ensure that it is accurately measuring the performance of all housing agencies so that it can reward high performers and hold troubled and substandard agencies accountable. We recommended that HUD (1) verify housing agencies' management operations certifications of major housing systems for accuracy and completeness and (2) ensure that it uses adequately verified housing agency performance information as the basis for planned performance bonuses and bonus points on applications for competitive grants.

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**Human Capital  
Weaknesses**

Under the 2020 Management Reform Plan, HUD has implemented significant organizational changes and contracted out substantial portions of the rental housing assistance programs' workload. But weaknesses in

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<sup>18</sup>*Public Housing: HUD Needs Better Information on Housing Agencies' Management Performance* (GAO-01-94, Nov. 9, 2000).

HUD's ability to oversee its multifamily and public housing properties have eroded mission capabilities.

In responding to our recent survey of HUD managers, about 51 percent of the multifamily managers reported that they have fewer staff than needed to carry out their activities. In addition, about 57 percent of the multifamily managers reported that the workload of their staff has increased over the past 2 years; about 74 percent attributed workload increases to new programs, and about 83 percent cited new regulations or initiatives. Managers in the Office of Public and Indian Housing, which oversees public housing agencies, expressed similar concerns. About 86 percent of these managers told us that they have fewer staff than they need to carry out the programs and activities in their area of responsibility. About 86 percent of these managers said that the workload had increased over 2 years ago, about 86 percent attributed this increase to new programs, and 97 percent cited new regulations and initiatives.

In our November 2000 report on measuring the performance of public housing agencies, we also reported that over 80 percent of HUD's public housing directors believed they have a less or much less than adequate number of field office staff to provide effective assistance to the housing agencies. When asked whether HUD has the tools and resources (number of staff; staff expertise; and training, travel, and contract funds) to ensure the accuracy and completeness of management operations certifications for major housing systems, 80 percent said HUD probably or definitely did not.

As we also reported in November 2000, public housing field officials told us they believe they are not adequately prepared to assist housing agencies because of insufficient field office staff, increasing workload, lack of staff qualifications and training, and insufficient training and technical assistance funds. HUD

headquarters acknowledged that the field offices needed additional training, in part because of the substantial turnover in staff in recent years and in part because of numerous new and revised program requirements resulting from recent public housing reforms. HUD has begun providing additional training, but the field offices face resource constraints. HUD officials told us that they doubt they will be able to increase field office staffing, and, as a result, HUD is evaluating the field offices' workload, focusing on reducing or eliminating responsibilities that may no longer be necessary.

In addition, to ease staffing shortages caused by staff reductions and streamlining under the 2020 Management Reform Plan, HUD awarded contracts in fiscal year 2000 for third-party contractors to administer about 22,000 project-based Section 8 housing assistance payments contracts, estimated to cost about \$200 million annually. By contracting for this work, HUD planned to free its staff for other functions, such as monitoring the multifamily portfolio. However, HUD awarded these contracts later than planned because of delays in announcing the request for proposals during the summer of 1999 and in reviewing the proposals. As a result, the first contracts were not awarded until February 2000, and as of November 2000, about 16,000 contracts had not yet been transferred to the Financial Management Center. Consequently, field office staff are still performing some of the tasks HUD had planned to shift to the Section 8 contractors.

Finally, as discussed in the section on HUD's single-family mortgage insurance programs, HUD's oversight of contractors and other entities, such as lenders, has suffered because of limits on the experience, qualifications, and number of HUD staff available for monitoring and other oversight functions. In the near future, we plan to look at HUD's capacity to oversee contractors.

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**Resolution Needed  
for Information and  
Financial  
Management  
Systems and  
Human Capital  
Issues**

To improve its management, HUD needs to resolve a number of challenges related to its information and financial management systems and its human capital. HUD needs to deploy a reliable financial management system that meets its program and financial management needs and complies with federal requirements. Moreover, in the human capital area, HUD needs to ensure that (1) its organizational realignment efforts are achieving the efficiencies envisioned, (2) it continues to develop a process to identify and justify its staffing requirements, and (3) staff are available and have the skills needed to carry out the work assigned. HUD's human capital problems can be seen as part of a broader pattern of human capital shortcomings that have eroded mission capabilities across the federal government. (See High-Risk Series: An Update (GAO-01-263, Jan. 2001) for a discussion of human capital as a newly designated governmentwide high-risk area.)

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**HUD Needs to  
Continue Efforts to  
Resolve Problems  
Related to  
Information and  
Financial  
Management Systems**

Since January 1999, HUD has initiated several actions to improve its information technology management and information and financial management systems. These include preparing a cost-benefit analysis of the 1997 strategy to complete its Financial Systems Integration (FSI) effort and using this analysis to define the project's scope and completion date, establishing a significant part of an information technology investment management process, implementing improvements to correct material internal control weaknesses in its systems, and continuing efforts to bring its financial management systems into compliance with federal requirements.

Although the Department has made progress, it continues to have problems. For example, HUD officials have determined that the financial management systems, developed under the recently completed FSI effort, do not meet all of its needs. As a result, the Department plans to replace the financial management systems, raising uncertainty as to whether the effort will be successful and timely. In addition, HUD experienced difficulties in implementing a departmentwide general ledger system, and as a result, the Inspector General could not complete the fiscal year 1999 financial statements audit within the statutory deadline.

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**HUD Has Taken  
Action to Address  
Information and  
Financial  
Management Systems  
Problems**

HUD's FSI effort, which involves the replacement of about 100 information and financial management systems, dates back to 1991. As we reported in December 1998, HUD revised its strategy to complete the FSI project in 1993 and again in 1997. However, because this effort was not supported by thorough analysis and did not receive adequate management and oversight, costs rose, and implementation was delayed. Moreover, HUD did not know when the effort would be completed, or at what cost, because it had not prepared detailed project plans or cost and schedule estimates for all components of the 1997 strategy.<sup>19</sup> We recommended that HUD prepare an estimate of the life-cycle costs and benefits of the overall 1997 FSI plan. In March 2000, Arthur Anderson, LLP, completed a cost-benefit analysis for the revised 1997 FSI strategy. The Chief Financial Officer (CFO) used this analysis to redefine the objective and scope of the FSI project, and HUD completed the redefined project on November 30, 2000.

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<sup>19</sup>*HUD Information Systems: Improved Management Practices Needed to Control Integration Cost and Schedule* (GAO/AIMD-99-25, Dec. 18, 1998).



HUD has coordinated with the Office of Management and Budget (OMB) and with us to establish an information technology investment management process that is expected to conform with industry best practices and legislative requirements. Management and oversight problems hampered the FSI effort because HUD did not have a disciplined, data-driven process to select, control, and evaluate its information technology investments. Furthermore, its process was not in conformance with industry best practices or with the requirements of the Clinger-Cohen Act of 1996 and the Paperwork Reduction Act of 1995. The Department developed selection procedures and criteria and established the Technology Investment Board Executive Committee, which selected projects and made funding decisions for fiscal years 2000 and 2001. The Department also recently developed control procedures and established a project management board, which has begun to review information technology projects that are under way. Finally, to complete its investment management process, HUD is beginning to develop evaluation procedures to determine whether its information technology investments are achieving the expected benefits and to identify opportunities for further improvement.

HUD has taken actions to address three systems-related material internal control weaknesses identified in the Inspector General's March 2000 audit report on HUD's financial statements. Two of these material weaknesses—FHA's budgetary and financial accounting controls must be improved and FHA's information systems must be enhanced to more effectively support FHA's business processes—are related to FHA's systems and were discussed in this report in the section on single-family mortgage insurance programs. The third material weakness is that HUD's financial systems are not fully compliant with federal financial systems requirements. In our October 2000 report on the status of HUD's actions to resolve serious internal control

weaknesses, we reported that HUD had actions under way or planned to bring its core financial systems into compliance with federal financial systems requirements. We concluded that HUD's strategy should help it continue to make progress in resolving all three of these material weaknesses.

In addition to those mentioned previously, some of the most significant improvements in HUD's development of financial management systems since March 1999, according to HUD CFO officials, include the following:

- HUD completed the implementation of the HUD Central Accounting and Program System (HUDCAPS) as the departmentwide general ledger and budget execution system.
- HUD implemented the prototype of the Empowerment Information System and data warehouse using selected Community 2020 and financial data.<sup>20</sup>

HUD also completed in October 2000 its latest departmentwide effort to evaluate whether its systems conform with federal financial systems requirements.<sup>21</sup> HUD reported that the number of nonconforming systems continues to decline and that at the end of fiscal year 2000, 12 of its 66 systems were nonconforming.

In January 1999, we reported that, according to HUD, it had completed all of its year 2000 renovations for both mission-critical and non-mission-critical systems. As of

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<sup>20</sup>Community 2020 is a Geographic Information Systems (GIS) software, with a database of 640 Census data elements, that shows where tax dollars are being spent in the community. According to HUD, the program was designed to facilitate citizens' involvement in the process of local community development.

<sup>21</sup>OMB Circular No. A-127 prescribes policies and standards for executive departments and agencies to follow in developing, operating, evaluating, and reporting on financial management systems.

March 1, 2000, HUD had experienced minimal disruptions from the millennium rollover, and no major systems failed, according to the Inspector General.

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**Some Systems  
Problems Persist**

After significantly revising the scope of its FSI project, HUD now plans to replace its financial management systems, creating some uncertainty about whether and when HUD will have a more modern, complete, and reliable financial management system. The CFO narrowed the objective and scope of the FSI project to completing a core general ledger that is compliant with federal financial systems requirements. Other components of the FSI project, specifically the Departmental Grants Management System and Enterprise Data Warehouse, were removed from and are no longer a part of the FSI project. Because HUD truncated the FSI project, as of November 30, 2000, it considered the project complete and the core general ledger system substantially compliant with federal financial systems requirements. The effectiveness of the actions taken by HUD will not be known until the fiscal year 2000 financial statement audit is completed in the spring of 2001.

While HUD considers its FSI project complete, the current financial management systems do not meet all of HUD's needs because they create burdensome manual reconciliation activities, increase the complexity and cost of maintenance, could cause diminished data control and integrity, and have inefficient system interfaces, according to HUD's Financial Management Vision statement. Accordingly, HUD now plans to replace its financial management systems, largely developed under the FSI effort, with a new system. This new plan is still in the early stages, and it reflects HUD's vision of developing a new integrated financial management system, but it leaves uncertain whether and when HUD will finally implement a system that will meet its program and financial management needs.

After issuing an unqualified opinion on HUD's fiscal year 1998 consolidated financial statements, the Inspector General was unable to issue an opinion the following year. The Inspector General reported in March 2000 that this was because HUD's fiscal year 1999 consolidated financial statements were not ready in time for the Inspector General to complete the audit by the statutory deadline. A new departmentwide general ledger system, implemented in fiscal year 1999, rejected or incorrectly posted numerous transactions, which then had to be manually researched and corrected. Furthermore, there was no software to help reconcile the general ledger cash accounts with the Department of the Treasury's account balance. According to the Inspector General, these implementation problems delayed HUD's financial reconciliation processes and resulted in numerous adjustments to make HUD's general ledger balance agree with Treasury's records. The Inspector General said there were 42 adjustments totaling about \$17.6 billion to adjust the fiscal year 1998 ending balance and 242 adjustments totaling about \$59.6 billion to adjust the fiscal year 1999 activity balance.

As a result of these problems, HUD was unable to prepare auditable financial statements and related disclosures in a timely manner, and the Inspector General could not complete the audit within the statutory time frames. The Inspector General also stated that the Department's core financial system did not fully comply with federal financial systems requirements because the departmental general ledger, HUDCAPS, was not updated with data from FHA each month and the data entry process was not timely or efficient. HUD has since taken actions to correct these problems, according to HUD officials. For example, HUD initiated studies aimed at resolving factors that contributed to the disclaimer, including its procedures for posting corrective adjustments during the year and its process for reconciling the funds balance with the Department of the Treasury's records. HUD officials also reported to us in May 2000 that they had completed the fiscal year 1999 reconciliation of funds balance with the U.S. Treasury. In addition, the Inspector General reported that a number of technical difficulties with interfaces between key transaction systems had been resolved.<sup>22</sup> The effectiveness of the actions taken by HUD will not be known until the fiscal year 2000 financial statements audit is completed in the spring of 2001.

A key component of HUD's FSI strategy was the Departmental Grants Management System (DGMS)—a departmentwide mixed management and financial information system that HUD expected to complete in July 2000. HUD has experienced problems with the development of this system, which was intended to support the Department's mission to restore the public trust by implementing a processing system that would consolidate all information on grants. HUD expected the

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<sup>22</sup>Statement of Susan Gaffney, Inspector General, U.S. Department of Housing and Urban Development, Tuesday, Sept. 26, 2000, before the Subcommittee on Housing and Transportation, U.S. Senate.

system to provide it with up-to-date information about competitive and entitlement grants and allow it to serve clients more efficiently. However, HUD suspended the system's development in June 2000 because it was concerned that delays in correcting software defects, as well as the software development approach, would not consistently meet all of the Department's needs or the needs of its business partners. HUD is recompeting the DGMS project. According to the Inspector General, \$5.3 million had been budgeted for the development of DGMS in fiscal year 1999 and \$6.3 million in fiscal year 2000.

In addition, the Inspector General reported in November 1999 that the initial efforts to develop DGMS were not cost-effective. In particular, the Inspector General reported that the option selected was the costliest and riskiest of the alternatives considered in the DGMS feasibility study. Moreover, the choice of this option led to the simultaneous development of another departmental system—the Integrated Disbursement and Information System (IDIS). The Inspector General concluded that this duplicative approach to supporting grants management would lead to higher development costs and greater risks of failure.

DGMS was intended to serve as a departmentwide information system that would be used to manage all of HUD's 51 grant programs, including its Community Planning and Development (CPD) grants to communities' operations. CPD's information and financial management system—IDIS— was designed to provide HUD's CPD operations with accurate, complete, and timely information on grantees' expenditures and program performance. We reported in April 1999 that these goals were not being achieved because of four significant problems.<sup>23</sup> Specifically, (1) the process for establishing and maintaining grant activity information was time-consuming and cumbersome and provided ample opportunity for major data entry problems, (2) major data entry problems were difficult to correct in IDIS, (3) IDIS did not readily enable grantees to accurately report income generated by grant-funded revolving funds (program income), and (4) grantees found it difficult to produce comprehensive and timely reports using IDIS. The Inspector General reported in May 2000 that several changes were being made to improve the IDIS software, but the changes were being implemented without adequate testing.<sup>24</sup> As a result, additional programming errors were being introduced, preventing CPD from achieving its goals.

In addition, in reviewing the decline in the number of systems that do not conform with federal financial systems requirements, the Inspector General reported in March 2000 that the CFO primarily relies on HUD's program offices to certify the systems' conformity. HUD does not require in-depth reviews of systems before

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<sup>23</sup>*Community Development: Weak Management Controls Compromise Integrity of Four HUD Grant Programs* (GAO/RCED-99-98, Apr. 27, 1999).

<sup>24</sup>*Integrated Disbursement and Information System*, Office of Inspector General (00-DP-166-0003, May 11, 2000).

reclassifying them from nonconforming to conforming. As a result, according to the Inspector General, systems were improperly classified as compliant and deficiencies were not identified. The Department intends to use a compliance review guide in fiscal year 2001, which provides substantially more detailed assessment criteria than were used in the past.

Finally, like many other federal agencies, HUD needs to continue to focus on improving its information technology management processes. HUD has continued its efforts to address the long-standing, fundamental management issues we raised in 1994 and 1998.<sup>25</sup> These issues involve (1) developing, integrating, and maintaining processes for strategic business and information resources management planning, enterprise architecture, and information technology investment management to routinely meet the Department's needs and (2) establishing sufficient security over the Department's sensitive information and systems. Resolving these issues is essential to achieving lasting improvements in the management of information technology and achieving consistently superior support for HUD's programs and operations.

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<sup>25</sup>*HUD Information Resources: Strategic Focus and Improved Management Controls Needed* (GAO/AIMD 94-34, Apr. 14, 1994) and *HUD Information Systems Improved Management Practices Needed to Control Integration Cost and Schedule* (GAO/AIMD-95-25, Dec. 18, 1998).



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**HUD Needs to  
Continue Efforts to  
Resolve  
Organizational and  
Staffing Problems**

In the past, we reported that an ineffective organizational structure and an insufficient number of staff with the necessary skills limited HUD in performing essential functions and contributed to our designation of HUD's programs as high risk. In 1997, HUD began to reorganize by function, following its 2020 Management Reform Plan, rather than continuing to operate strictly within individual programs. As noted in the previous sections on HUD's single-family mortgage insurance and rental housing assistance programs, HUD transferred many staff from its field offices to various hubs, program centers, and specialized and nationwide centers. HUD has substantially completed this transfer and implemented its organizational realignment to the extent that it has begun to achieve some results. HUD is also implementing a new process to improve its estimation of resource needs and allocation of staff, and it has made additional funding available for training and travel. However, even before it began its staffing and allocation process, HUD created the position of Community Builder to provide hands-on service and outreach to communities. HUD currently has over 600 Community Builders, even though, as we reported in September 1999,<sup>26</sup> the Department has not compared the program's costs and benefits to determine whether the benefits are worth the costs of hiring and training the Community Builders.

However, not all of the results envisioned by the 2020 plan have yet been realized. Problems remain related to the operations of some of the reorganized activities, particularly in terms of workload. Moreover, insufficient staffing and limited travel funds continue to affect HUD in carrying out its mission. Our recent telephone survey

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<sup>26</sup>HUD's Fiscal Year 2000 Budget Request: Additional Analysis and Justification Needed for Some Programs (GAO/RCED-99-251, Sept. 3, 1999).

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of HUD managers indicated that they believe they do not have enough staff and that their workload has increased, rather than decreased as expected.

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**HUD Has Taken  
Action to Address  
Staffing Problems**

As of September 2000, HUD had 8,951 full-time employees administering its programs and functions, somewhat below its fiscal year 2000 authorization of 9,300 full-time employees. HUD requested additional staff in its budget submissions for fiscal years 2000 and 2001, but the Congress declined to provide additional resources, in part because of concerns that HUD lacks a reliable resource management system to determine the appropriate level of staff. In its annual performance plan for fiscal year 1999, submitted to the Congress in March 1998, HUD noted that it lacked departmental systems for measuring work and reporting time and that it lacked a single integrated system to support resource allocation. The absence of this capability concerned the Congress, which requested that NAPA examine HUD's practices for estimating human resource needs. For the past 2 years, NAPA and HUD have worked together to design and pilot-test a methodology for a resource management system. In August 2000, HUD began to implement the new process in three phases, the last of which is scheduled to be completed in December 2001.

Since January 1999, HUD has also taken steps designed to ensure that its employees have the skills and knowledge to carry out their functions. During fiscal year 2000, HUD greatly increased its expenditures for technical and management training, spending about \$5.9 million compared with \$1.7 million in fiscal year 1999. According to our telephone survey of HUD managers, most were satisfied with the training available to them and their staff.<sup>27</sup> Almost three-quarters of the managers rated HUD's current training as excellent or good and said the training was better now than it was 2 years ago.

Overall, the managers responding to our current survey as well as our 1996<sup>28</sup> survey expressed satisfaction with their staff's skills. The vast majority in the current survey (89 percent) said they were very satisfied or generally satisfied with their staff's skills, and nearly all (95 percent) said their staff's skills had improved greatly or somewhat. In the current survey, a higher proportion of the managers rated their staff's individual skills as excellent or good, and a smaller proportion classified their staff's skills as fair or poor. The ratings covered interpersonal skills, knowledge of new programs, knowledge of information systems, technical skills, and knowledge of existing and new regulations. These results are particularly noteworthy because, as we

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<sup>27</sup>We conducted a telephone survey of managers of HUD's major programs in selected field offices and in six specialty centers. Our survey, conducted during September and October 2000, asked the managers for their views on current staffing skills, training, and workload in their areas of responsibility. The survey included 110 field office managers in three major program areas (multifamily housing, community planning and development, and public housing) at 39 offices. It also included 45 managers in six specialty centers—Homeownership, REAC, Troubled Agency Recovery, Enforcement, Financial Management, and Grants Management—to reflect the current organization.

<sup>28</sup>*HUD: Field Directors' Views on Recent Management Initiatives* (GAO/RCED-97-34, Feb. 12, 1997). In 1996, we conducted a similar survey of 155 HUD field office managers. Specialty centers did not exist at that time.

reported in January 1999, field office managers told us then that some newly placed staff lacked the specific program knowledge necessary to do their jobs, whereas our current survey shows that 91 percent of the field office managers were satisfied with their staff's skills.

Between fiscal year 1998 and fiscal year 2000, HUD's overall travel budget increased from about \$17.8 million to about \$22 million. The majority of the program offices or areas experienced increases, although a few experienced decreases. Despite increases in travel funds, HUD field offices continue to report that they lack sufficient travel resources, as noted in the section on HUD's single-family mortgage insurance programs.

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**Some Organizational  
and Staffing  
Problems Persist**

According to reports that we and the Inspector General have issued, our recent audit work, and the results of our telephone survey, HUD's reorganization has not proceeded exactly as planned, and imbalances in workload have occurred at several specialty centers and in some of the field offices.<sup>29</sup> In addition, insufficient staffing and the need to increase training continue to affect HUD's ability to carry out its mission efficiently and effectively. The managers we surveyed reported that training and staff skills have generally improved, but the managers also believe that training should be increased.

The workload in the related field offices remains larger than planned, in part because some responsibilities remain to be transferred to the centers and in part because the field offices have acquired new responsibilities. In addition to handling workload that has not moved to the centers as soon as planned, the field offices have acquired additional work as new programs, regulations, and management initiatives have

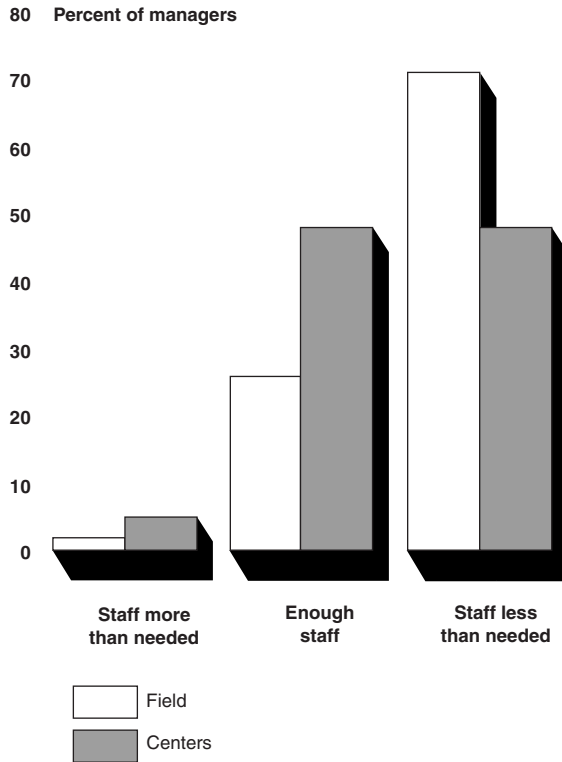
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<sup>29</sup>The telephone survey and specialty center workload issues are described in the overview section and program sections, respectively.

created new responsibilities. The field offices have not received additional staff to carry out these new responsibilities. About 79 percent of the HUD field office managers we surveyed reported increases in their workload over the last 2 years.

In addition to workload imbalances, HUD centers and field offices have experienced problems related to insufficient staffing. Our recent telephone survey of HUD managers found that most managers (65 percent) at the centers and field offices believe they do not have enough staff to carry out their programs and activities. A higher proportion of field office managers (71 percent) than center managers (48 percent) said they do not have sufficient staff to carry out programs and activities. The 1996 survey, conducted before HUD implemented its reform actions, found that 77 percent of the managers believed they lacked sufficient staff to carry out programs and activities effectively. Figure 1 summarizes HUD managers' views on the adequacy of their staffing levels.

Figure 1: Field Office and Specialty Center Managers' Views on Adequacy of Staffing Levels



Source: GAO's 2000 survey of HUD managers.

Although the majority of the managers reported being satisfied with the training HUD provides, managers at both the centers and field offices agreed that HUD should increase training in several areas. Specifically, managers stated that training should be increased in the areas of information systems (75 percent), program regulations and changes (72 percent), technical job skills (71 percent), and interpersonal skills (59 percent).

Center managers were more critical of HUD's training than were field office managers. About 59 percent of center managers rated HUD's training as excellent or good, compared with 80 percent of field office managers. In addition, 47 percent of center managers stated that HUD's training is better than it was 2 years ago, compared with 81 percent of field office managers. We believe this difference in managers' views on HUD's training is consistent with the fact that the centers are fairly new and center staff may require more training to learn the specialized skills needed to do their jobs.

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