DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

April 6, 2018

The Honorable Christy Goldsmith Romero
Special Inspector General
for the Troubled Asset Relief Program
1801 L Street, N.W., 4th Floor
Washington, D.C. 20036

Re: Audit Report Relating to Hardest Hit Fund Administrative Costs

Dear Ms. Romero:

I write in response to the August 25, 2017 Audit Report (Report) from the Special Inspector General for the Troubled Asset Relief Program (SIGTARP) concerning administrative costs funded through the Treasury's Hardest Hit Fund (HHF). On August 24, 2017, we provided an official response to the draft version of the Report, in which we stated our intention to consider carefully the Report's 30 recommendations. We also requested from SIGTARP a detailed list of the transactions comprising the figures in those recommendations. SIGTARP provided us with that information on September 26th, October 11th, and October 25th. We have since completed our review and, with this letter, we summarize Treasury's criteria for evaluating administrative costs and provide our response to SIGTARP's specific recommendations.

I. Treasury's Criteria for Evaluating Administrative Costs

Treasury established the Hardest Hit Fund in February 2010, to help prevent foreclosure and stabilize housing markets in areas hardest hit by the housing crisis. To implement HHF, Treasury committed $9.6 billion under contracts with state housing finance agencies (together with certain designated entities, the HFAs) in 18 states and the District of Columbia. HFAs use the funds to design and implement programs tailored to the specific needs and conditions of their respective communities. Approximately 90 percent of HHF funding is used to assist struggling homeowners directly—*e.g.*, payments toward their monthly mortgage obligations—or to demolish blighted homes. HFAs use the remainder to cover the administrative costs they incur to implement the program.

As SIGTARP acknowledges in the Report, Treasury "set significant limits in its HHF contracts with state agencies" in an effort to "ensure that [HHF] follows TARP law and funds reach their intended recipients."[1] This includes requiring that administrative costs comply with Office of Management and Budget standards and principles (the OMB cost principles), as well as a summary budget approved by Treasury.[2]

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[1] Report at 1.
[2] These principles were initially set forth in OMB Circular A-87, which can be viewed at https://www.gpo.gov/fdsys/pkg/CFR-2012-title2-vol1/pdf/CFR-2012-title2-vol1-part225.pdf. In December 2016,

As a basic condition of allowability, the OMB cost principles require that administrative costs be both necessary and reasonable for the HFAs' performance of the HHF contracts.[3] Other basic conditions include, but are not limited to, being allocable to the HHF contract—as opposed to other activities of the HFA unrelated to HHF—and adequately documented.[4] The OMB cost principles also provide detailed requirements governing the allowability of specific types of costs, as discussed below in further detail.

II. Recommendations to Recover $2.2 Million from 19 HFAs

In Recommendation Numbers 5 through 25, 28, and 30, SIGTARP recommends that Treasury recover $2.2 million in costs incurred by the 19 HFAs and funded through HHF.[5] This amount is comprised of thousands of individual transactions that fall into one of six broad categories, as discussed in more detail below. In summary, Treasury required the HFAs to reimburse HHF for $656,141 (or 29%) of the $2.2 million questioned by SIGTARP, as follows:

Categories	SIGTARP Recommendation	Amount Recovered	Percentage Recovered
Employee Compensation	$ 1,240,567	$ 327,195	26.4%
Office Facilities and Equipment	$ 395,456	$ 217,570	55.0%
Homeowner Application System	$ 382,750	$ 22,300	5.8%
Meetings and Conferences	$ 120,996	$ 44,251	36.6%
Legal Expenses	$ 90,629	$ 38,974	43.0%
Gifts and Promotional Items	$ 5,851	$ 5,851	100.0%
Total	**$ 2,236,249**	**$ 656,141**	**29.3%**

Although Treasury determined that recovery of the remaining costs identified by SIGTARP was not warranted, Treasury will continue to monitor the HFAs' compliance with HHF program requirements and, if violations are found, take remedial action as appropriate.

Employee Compensation

SIGTARP questioned $1,240,567 of costs relating to compensation paid to or on behalf of HFA employees and other staff that support HHF programs.[6] Such compensation includes incentive-based compensation, unemployment compensation, severance pay, and certain other fringe benefits. Each of these types of costs is expressly allowable under OMB cost principles,

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Treasury updated its contracts to instead adopt Subpart E of 2 C.F.R Part 200, OMB's uniform cost principles for Federal awards, the most up-to-date requirements applicable to state and local governments, non-profit organizations, and other non-Federal recipients of Federal funds.

[3] *See*, *e.g.*, 2 C.F.R. 200.403.

[4] *Id*.

[5] Although the Report states that HFAs "charged $3 million in unnecessary expenses to the Hardest Hit Fund," the cited recommendations—when aggregated—state that Treasury should recover at least $2.2 million of that amount. Report at 1, 70-75.

[6] In some cases, staff were engaged as contractors, rather than as employees.

provided that the costs meet the basic conditions of allowability and satisfy other terms and conditions stated therein.[7] These compensation costs often constitute taxable income, and form part of the individual's overall compensation package, together with their salaries and wages.

In general, it is necessary for HFAs to compensate staff for services rendered in support of HHF. The form of that compensation may differ for a number of reasons. For example, structuring a portion of an employee's compensation as incentive-based, rather than salaried, can increase productivity by tying compensation to actual deliverables or desired results. It can also be used to retain personnel with invaluable institutional knowledge, thus saving resources that would otherwise be used to recruit and train replacement staff. Alternatively, the law may require some types of compensation, such as the unemployment compensation SIGTARP questioned.[8] In addition, with respect to severance pay—which is paid when an individual's employment is terminated—the HFAs typically obtained a release of claims, which reduces the risk of frivolous litigation, and related costs that may otherwise be allowable.[9]

Another form of compensation is fringe benefits, defined in the OMB cost principles as "allowances and services" provided by employers in addition to regular salaries and wages.[10] In that regard, some HFAs chose to subsidize the cost of bus passes or parking for HHF support staff. This practice was prevalent in geographic areas where the HFA determined that parking was cost-prohibitive for workers, and not already built into the rent associated with the HFAs' office space. Several HFAs reported having procured these benefits at a discounted, group rate, which was less costly than increasing individual salaries and wages to cover the related costs.

As another example of fringe benefits, one HFA instituted a health and wellness incentive program to improve employee productivity by promoting employee mental and physical well-being. This included contributing $30 per month toward a gym membership, on the condition that the employee meet minimum exercise requirements. The OMB cost principles expressly allow costs incurred for the improvement of employee health and employee performance, two factors which can be viewed as linked.[11] Indeed, the U.S. Office of Personnel Management (OPM) acknowledges that worksite health and wellness programs—including those that promote physical activity—can "produce organizational and employee benefits … such as … increased productivity" and encourages Federal agencies to develop such programs.[12]

Ultimately, the HFAs reimbursed the Hardest Hit Fund for $327,195 of the compensation costs questioned by SIGTARP. In many cases, Treasury disallowed the costs, either because the HFA was unable to provide sufficient documentation to demonstrate compliance with the OMB cost principles, or because the costs were deemed not allocable to HHF. In some cases, the HFA

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[7] *See*, *e.g.*, 2 C.F.R. 200.430 and 200.431.

[8] Each of the HFAs reported that the payments in question were made in accordance with state law. *See*, *e.g.*, Section 505 of Chapter 657 of the *Oregon Revised Statutes.*

[9] As the OMB cost principles state, "the Federal Government recognizes its obligation to participate, to the extent of its fair share, in any specific [severance] payment." 2 C.F.R. 200.431(i)(2)(ii).

[10] *See, e.g.*, 2 C.F.R. 200.431(a).

[11] *See, e.g.*, 2 C.F.R. 200.437(a).

[12] *See* https://www.opm.gov/policy-data-oversight/worklife/health-wellness (last accessed Apr. 4, 2018).

voluntarily repaid the Hardest Hit Fund, in which case Treasury did not make a determination as to the allowability of the underlying costs.

Office Facilities and Equipment

SIGTARP questioned $395,456 of costs relating to maintaining office facilities and equipment utilized by HFA staff in support of HHF. This includes, for example, the costs of rent, building improvements, computers, furniture, state-owned motor vehicles, office supplies, and utilities. Each of these types of costs is expressly allowable under the OMB cost principles, on the terms and conditions stated therein.[13]

In general, it is necessary for HFAs to maintain office space where HHF support staff can work, and to furnish and otherwise equip that space for such use. In one recommendation, SIGTARP questioned an HFA's practice of "paying rent to itself" in a building that it owned, three years after the HFA closed its HHF office. Treasury determined that the HFA had relocated its HHF staff to its own building, following the expiration of the lease where it previously had maintained its HHF office. Following the relocation, the HFA continued to operate its HHF programs from its own building. The OMB cost principles expressly allow the HFA to be compensated for the use of its building by charging to HHF what is referred to as a "use allowance."[14]

As to other costs in this category, HFAs ultimately reimbursed the Hardest Hit Fund for $217,570. In most cases, Treasury determined that the costs were not allocable to HHF or exceeded the amount permitted under the OMB cost principles. In some cases, the costs had already been reimbursed to the Hardest Hit Fund prior to the issuance of the Report.

Homeowner Application System

SIGTARP questioned $382,750 of costs relating to a web-based portal that homeowners can use to apply for HHF assistance in some states. This technology enables the HFAs to collect and process the homeowner's application materials, to retain those materials in a retrievable manner as required under the HHF contracts, and to analyze homeowner data in an effort to improve program performance. Each of these functions is essential to the successful implementation of HHF programs.

Included within this amount is SIGTARP's recommendation that Treasury recover $258,333 from one HFA, which SIGTARP described as having purchased a "multi-year, prepaid contract" to use the portal. The HFA purchased a license that runs through 2020, the scheduled end of HHF.[15] By purchasing a multi-year license, as opposed to an annual license, the HFA was able to procure the technology at a significant discount. Had the HFA purchased annual licenses for

[13] *See, e.g.*, 2 C.F.R. 200.436, 200.437, 200.439, 200.452-453, and 200.465.
[14] *See* OMB Circular A-87, App. B, section 11.a.
[15] Treasury determined that the HFA has thus far operated HHF programs at all times during the license term. If historical trends continue, the HFA has sufficient funding to continue operating HHF programs through at least December 31, 2020.

the same period of time, Treasury estimates that the cost could have been more than twice as much. Accordingly, the HFA's approach resulted in cost savings for the Federal taxpayer.

With respect to other costs questioned by SIGTARP, Treasury determined that $22,300 was not allocable to HHF, and required the applicable HFA to reimburse the Hardest Hit Fund accordingly.

Meetings and Conferences

SIGTARP questioned $120,996 of costs relating to food and beverages, and other incidental costs of meetings, conferences, and other events. The cost of meals is expressly allowable under the OMB cost principles, when the meal is incidental to a meeting or conference, the primary purpose of which is the dissemination of technical information about the Federal award (here, HHF).[16] Meals may be provided, for example, when lengthy meetings extend over the lunch hour or another regular mealtime, or in connection with an all-day conference where participants are expected to remain on the premises. Conversely, the cost of meals is expressly prohibited if provided for entertainment purposes, including amusement, diversion, or social activities.[17]

In order to apply the foregoing criteria, Treasury collected and reviewed documentation from the HFAs—such as meeting agendas and presentation materials—with respect to each event questioned by SIGTARP. Based on that documentation, Treasury determined whether the event was a meeting or conference, whether the primary purpose of the meeting or conference was the dissemination of technical information about HHF, and whether the provision of meals was reasonable based on the facts and circumstances. If there was sufficient documentation to show that all of these criteria were met, Treasury allowed the associated costs. If not, or in the absence of sufficient documentation, Treasury deemed the costs to be unallowable.

Treasury found numerous events that met the criteria set forth in the OMB cost principles. For example, some HFAs conducted lengthy training sessions for large groups of housing counselors (*e.g.*, 50-100 individuals), where the HFAs educated counselors about the detailed eligibility, underwriting, and other state-specific criteria of HHF programs.[18] As another example, some HFAs arranged meetings or conferences with legislative staff, mortgage servicers, or other program partners. The HFAs disseminated technical information about HHF at these events, in an effort to improve the reach and effectiveness of HHF programs in their respective states. In order to minimize scheduling conflicts, some of these events were held during the breakfast hour. Other events lasted for most or all of the business day, such as when out-of-state attendees would travel to the HFA. In such cases, HFAs would arrange for bagels, sandwiches, or other modest meals to be brought in from nearby restaurants or catering services, in order to maximize the amount of time available to work on HHF matters.

Following its review, Treasury ultimately required HFAs to reimburse the Hardest Hit Fund for $44,251 of the questioned costs. In many of these cases, Treasury determined that the events did

[16] *See, e.g.*, OMB Circular A-87, App. B., s.27.
[17] *See, e.g.*, OMB Circular A-87, App. B., s.14.
[18] Housing counselors help homeowners complete and submit applications for HHF, at no cost to the homeowner.

not meet the criteria required for costs associated with meetings and conferences, or disallowed costs because the HFA could not provide sufficient documentation for Treasury to make a determination. In other cases, the HFAs voluntarily repaid the Hardest Hit Fund, in which case Treasury did not make a determination as to the allowability of the underlying costs.

Legal Expenses

SIGTARP questioned $90,629 of costs relating to legal fees and settlement payments involving former employees that supported HHF. The OMB cost principles expressly allow the cost of services provided by members of a profession—such as attorneys—but expressly disallow costs associated with certain types of litigation or settlements.[19] Treasury reviewed documentation associated with the costs, and determined that only $53,753 had actually been charged to HHF. Treasury further disallowed $38,974 of those charges, and determined that most of the disallowed charges had already been reimbursed prior to the issuance of the Report. Treasury required the applicable HFAs to reimburse the Hardest Hit Fund for the balance.

Gifts and Promotional Items

SIGTARP questioned $5,851 of costs relating to items described as gifts, all of which has been reimbursed to the Hardest Hit Fund. These costs consisted largely of plastic tumblers, t-shirts, and other memorabilia provided at HHF-sponsored promotional events. Although the OMB cost principles do permit some costs associated with advertising and promotion of HHF programs, the costs of promotional items and memorabilia, including gifts and souvenirs, are expressly prohibited.[20] In some cases, the HFA voluntarily repaid the Hardest Hit Fund, and Treasury did not make a determination regarding the underlying cost.

III. Recommendation to Recover $8.1 Million from NAHAC

In an earlier report dated September 9, 2016, SIGTARP recommended that Treasury recover from the Nevada Affordable Housing Assistance Corporation (NAHAC) approximately $8.2 million in administrative costs.[21] After a thorough review, Treasury determined that $82,173 of these costs were unallowable and recovered those funds. Treasury explained its conclusions in a letter dated January 19, 2017, and we attach a copy of that letter for your reference. SIGTARP has since recommended again that Treasury recover the remaining $8.1 million. For the reasons set forth in our prior letter, Treasury maintains that recovery of these costs is not warranted at this time. Still, Treasury will continue to monitor NAHAC's compliance with HHF program requirements and, if violations are found, take remedial action as appropriate.

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[19] *See, e.g.*, 2 C.F.R. 200.435, 200.441 and 200.459.
[20] *See, e.g.*, 2 C.F.R. 200.421. *See also*, 2 C.F.R. 200.445.
[21] We note that this amount is a net figure, eliminating double-counting of transactions in SIGTARP's individual recommendations, which sum to $10.1 million.

SIGTARP's remaining recommendations are already addressed by Treasury's existing procedures, which are summarized in our prior responses to you dated January 19, 2017 and August 24, 2017, copies of which are attached for your reference.

We also wish to address SIGTARP's view that Treasury should apply additional criteria in its evaluation of administrative costs, namely, those standards described in a memorandum from Treasury's Office of the General Counsel in 2010. For context, the referenced memorandum evaluated whether the Troubled Asset Relief Program (TARP) appropriation was available to fund certain legal aid services in connection with HHF. The memorandum applied the Comptroller General's "necessary expense" doctrine, which requires that the cost in question be necessary or incident to the implementation of an express statutory purpose—in this case, facilitating loan modifications that prevent avoidable foreclosure, pursuant to the Emergency Economic Stabilization Act of 2008 (as amended, EESA), TARP's governing statute.[22] The current HHF contracts satisfy this doctrine because their sole purpose is to implement the loan modification programs authorized under EESA.[23] The reimbursement of the HFAs' administrative costs as part of the consideration due under those contracts is thus a necessary expense, provided such costs satisfy OMB cost principles and other contractual requirements.[24]

We are committed to maximizing the efficiency and effectiveness of Treasury's programs and reducing the potential for waste and abuse as we continue to wind down TARP. To that end, we note that, since the issuance of the Report, some HFAs have conducted their own reviews of administrative costs. The HFAs have collectively volunteered to repay $456,307 in administrative costs not identified in the Report. This primarily has consisted of compensation inadvertently charged to HHF by one HFA, following the re-assignment of personnel that previously supported HHF. Treasury has confirmed that these additional amounts have also been repaid to HHF.

Please feel free to contact Treasury's Office of Financial Stability at (202) 622-4421 if you have any questions about this letter.

Sincerely,

Lorenzo Rasetti

Lorenzo Rasetti
Chief Financial Officer
Office of Financial Stability

Enclosures

[22] "[T]he Secretary may use loan guarantees and credit enhancements to facilitate loan modifications to prevent avoidable foreclosures." 12 U.S.C. 5219(a)(1).
[23] All HHF programs are designed to prevent foreclosure and stabilize housing markets by facilitating loan modifications, and thus constitute loan modification programs.
[24] *See, e.g.*, 55 Comp. Gen. 652 (1976).

Attachments

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

January 19, 2017

The Honorable Christy Goldsmith Romero
Special Inspector General
for the Troubled Asset Relief Program
1801 L Street, N.W., 4th Floor
Washington, D.C. 20036

Re: September 9, 2016 Audit Report Relating to Hardest Hit Fund Nevada

Dear Ms. Romero:

I write in response to the September 9, 2016 Audit Report (Report) from the Special Inspector General for the Troubled Asset Relief Program (SIGTARP) concerning the Hardest Hit Fund (HHF) program in Nevada. The Department of the Treasury (Treasury) appreciates SIGTARP's analysis of administrative expenditures incurred by the Nevada Affordable Housing Assistance Corporation (NAHAC), which administers HHF programs in Nevada. We previously provided an official response to the draft version of the Report on September 8, 2016, in which we stated our intention to carefully consider the recommendations SIGTARP outlined in the Report. With this letter, we provide Treasury's response to those recommendations.

Treasury is committed to preventing waste, fraud, and abuse in HHF programs. Since the launch of HHF, Treasury has implemented procedures to control administrative spending and ensure that taxpayer funds are spent responsibly. Under HHF contracts, administrative expenses are subject to federal cost principles issued by the Office of Management and Budget (OMB), as well as to an administrative budget approved by Treasury. Treasury evaluates compliance with these requirements, on a sample basis, in regular, on-site compliance reviews. States are also required to implement internal controls to help ensure that HHF programs are implemented effectively, efficiently and in compliance with Treasury's contract. These internal controls are evaluated by Treasury during its on-site reviews, and they are independently verified on an annual basis. In addition, Treasury requires each state to submit regular financial reports, which include information about the state's administrative spending. Treasury uses these reports and the results of its compliance reviews to monitor the performance of HHF programs and requires states to take corrective action as needed.

We summarize below our careful consideration of SIGTARP's recommendations and the actions we have taken, or will take, in response.

Structure and Oversight of Nevada's HHF Program

We agree with SIGTARP that the Nevada Housing Division (NHD), a division of the Department of Business and Industry of the State of Nevada, should directly oversee the administration of Nevada's Hardest Hit Fund program. Following Treasury's request in December 2015, NAHAC's board of directors was restructured to vest control with representatives of the State of Nevada, including NHD. Under this new leadership, the board replaced several members of NAHAC's senior management team and made other organizational, operational, and fiscal changes to improve the administration of HHF Nevada. These include, for example: reducing permanent staff through attrition and relying on temporary staff to address short-term hiring needs; closing a satellite office; obtaining support services from organizations that have demonstrated success with HHF programs in other states; increased review by trained personnel prior to payment of invoices; reducing administrative costs by outsourcing property value assessments and analytics; adopting workflows and processing systems similar to those utilized by other HHF states to streamline the homeowner application process; adjusting program requirements to increase the reach and effectiveness of HHF assistance; and increasing coordination with industry stakeholders, including housing counseling agencies and mortgage servicers.

With respect to SIGTARP's specific recommendation that NAHAC be removed from the program entirely, we carefully reviewed this recommendation and considered the administrative burdens—both in terms of cost and delay—that such an action would impose. We ultimately concluded that the steps taken to restructure NAHAC achieve the purpose of SIGTARP's recommendation without imposing undue burdens on program administration.

Allocation of States' Costs Between HHF and Non-HHF Programs

We agree with SIGTARP about the importance of allocating states' costs between HHF and non-HHF programs. Indeed, Treasury requires states to provide third-party documentation supporting administrative expenses charged to HHF, as part of its on-site compliance reviews. Treasury has not, and will not, accept block bills or other documentation in support of HHF charges where the amount expended for HHF cannot be ascertained. Moreover, states participating in HHF are required to allocate overhead costs—*e.g.*, salaries, rent and utilities—between HHF and non-HHF programs. Treasury evaluates each state's cost-sharing methodology as part of its routine on-site compliance reviews, and obtains other supporting documentation as needed. We believe that Treasury's existing requirements and oversight in this area safeguard against HHF funds being used for non-HHF purposes.

We carefully considered SIGTARP's corresponding recommendations, including that Treasury seek to recover 100 percent of NAHAC's overhead costs charged to HHF Nevada in 2014 and 2015 (approximately $7.5 million). As part of Treasury's compliance review of HHF Nevada, we reviewed NAHAC's financial statement disclosures, conducted interviews and obtained written statements from knowledgeable personnel, and performed other procedures that provided insight into NAHAC's operations. We ultimately concluded that NAHAC did not operate programs other than HHF in 2014 and 2015, and as such NAHAC's allocation of 100% of its overhead to HHF during these years was appropriate.

Administrative Expenses Relative to Homeowner Assistance

We agree with SIGTARP that administrative expenses should be reasonable in light of the objectives of HHF. As noted above, Treasury has implemented procedures designed to control administrative spending and ensure that taxpayer funds are spent responsibly. These include, among other things, monitoring administrative spending and requiring states to take corrective actions as needed. In Nevada's case, Treasury issued a memorandum to NAHAC and NHD in December 2015, noting the disparity between NAHAC's administrative expenses and its assistance of homeowners. Treasury also requested that NHD and NAHAC take immediate action to improve the performance of Nevada HHF programs. In response, NHD and NAHAC took steps to bring HHF Nevada under NHD's direct oversight and make additional administrative improvements, as described above in greater detail.

SIGTARP made several specific recommendations calling for Treasury to assess the reasonableness of administrative expenditures relative to the number of homeowners admitted and/or amounts disbursed for homeowner assistance over a given period. In particular, SIGTARP recommended that Treasury recover $2.2 million in administrative expenses, which SIGTARP calculated as the amount by which administrative expenses per homeowner admitted in 2015 exceeded those in 2013. SIGTARP also recommended that Treasury suspend administrative funding and take other actions when a state's administrative expenses equal, exceed or are disproportionate to the amount disbursed for homeowner assistance on a quarterly basis.

We note that administrative expenses in one quarter may not align with the number of homeowners approved or the amount of assistance disbursed in the same quarter for a variety of reasons. For example, while some costs will decline with the number of homeowners assisted, other costs—such as salaries, rent and utilities—will remain fixed. This is apparent in NAHAC's case, where administrative expenses declined substantially from 2013 to 2015, although not in direct proportion to the number of homeowners helped.[1] In addition, administrative expenses that do vary with the number of homeowners assisted—such as the cost of in-take counseling and lien recordation fees—are not always incurred in the same quarter that the homeowner's assistance is disbursed. Rather, such costs are often incurred before any assistance is disbursed, and disbursements often occur in monthly installments over several subsequent quarters.

For these reasons, we do not believe administrative costs should be disallowed and recovered solely by comparison to the number of homeowners admitted or amount of assistance disbursed each quarter. We will, however, continue to monitor administrative spending and, should we note a significant disparity, require that states take steps to improve their program administration.

Additional Compliance Reviews and Corrective Actions

Treasury is committed to the responsible stewardship of taxpayer dollars, and we agree with SIGTARP that Treasury should seek to recover amounts expended in violation of HHF program requirements. As noted above, administrative expenses in HHF are subject to federal cost principles issued by OMB and an administrative budget approved by Treasury. Treasury is in

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[1] NAHAC's administrative expenses in 2015 were roughly half of what they were in 2013. https://www.treasury.gov/initiatives/financial-stability/reports/Pages/Housing-Finance-Agency-Aggregate-Report.aspx

the process of evaluating the Nevada HHF transactions identified in several of SIGTARP's recommendations—totaling approximately $350,000—and will seek recovery as appropriate. Treasury also agrees that the types of transactions for which it should seek recovery include, but are not limited to, non-business related travel and entertainment, goods and services for employees' personal use, charges not related to HHF, charges not supported by documentation, charges in violation of NAHAC policies, and legal costs not required for the proper administration of HHF.

Treasury also agrees with SIGTARP that it should take additional steps to monitor administrative spending in HHF. Accordingly, in addition to continuing its regular, on-site compliance reviews of HHF programs administered by each the 18 states and the District of Columbia, Treasury will enhance its procedures for evaluating administrative expenses. This will include increasing the sample size for types of expenses that present a higher risk of non-compliance. Treasury's next review of HHF Nevada will begin in early 2017.

Additionally, Treasury agrees with SIGTARP that states should take corrective actions in a timely fashion. Treasury currently requires HHF states to respond to Treasury's compliance findings within 30 days after issuance of Treasury's compliance report. Treasury's observations are not closed until corrective actions have been implemented and validated by Treasury. Compliance findings and corrective actions are considered in processing drawdown requests.

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We thank SIGTARP for bringing these important matters to our attention. We look forward to working with SIGTARP and its staff to maximize the efficacy of Treasury's programs and reduce the potential for waste and abuse as we continue to wind down the Troubled Asset Relief Program. Please feel free to contact Treasury's Office of Financial Stability at (202) 622-4421 if you have any questions about this letter.

Sincerely,

Mark McArdle
Deputy Assistant Secretary for Financial Stability

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

August 24, 2017

The Honorable Christy Goldsmith Romero
Special Inspector General
for the Troubled Asset Relief Program
1801 L Street, NW, 4th Floor
Washington, DC 20036

Dear Ms. Romero:

I write in response to the Special Inspector General for the Troubled Asset Relief Program's (SIGTARP) draft report of August 10, 2017 (the Draft), regarding certain administrative expenses funded through Treasury's Housing Finance Agency Innovation Fund for Hardest Hit Housing Markets (the Hardest Hit Fund, or HHF). Treasury takes very seriously its responsibility as a steward of taxpayer funds, and we appreciate SIGTARP's oversight as we continue to wind down the Troubled Asset Relief Program (TARP).

HHF is a $9.6 billion program created in February 2010 to help struggling homeowners avoid foreclosure and stabilize housing markets in areas hit hardest by the housing crisis. Funding is used by housing finance agencies (together with certain affiliates, HFAs) in 18 states and the District of Columbia, to design and implement HHF programs tailored to the specific needs and conditions of local communities. To date, HFAs have established 88 programs under HHF, which have collectively assisted more than 305,000 homeowners and helped to remove more than 17,000 blighted properties.

Treasury is committed to preventing waste and abuse in HHF and ensuring that taxpayer funds are used responsibly. We appreciate SIGTARP's thorough review of administrative expenses incurred by the HFAs and funded through HHF over the last seven years. In the Draft, SIGTARP recommends that Treasury recover certain of those expenditures and implement a series of controls to prevent unnecessary spending in the future. We agree that Treasury should recover amounts expended in violation of program requirements and take other actions to control administrative spending. With this letter, we describe the steps Treasury has taken to limit administrative expenses based on standards established by the Federal government and enforce those limitations through periodic compliance reviews. We will carefully consider the information and recommendations contained in the Draft and respond to each of SIGTARP's recommendations in a subsequent letter, once we have completed that review.

I. Treasury Requires that HHF Administrative Expenses Comply with Federal Cost Principles.

As SIGTARP's Draft acknowledges, Treasury "set significant limits in its HHF contracts with [HFAs]" in an effort to "ensure that the HHF follows TARP law and funds reach their intended recipients…."[1] These contracts impose a number of requirements with respect to administrative expenses in particular, including that such expenses must comply with standards and principles prescribed by the Office of Management and Budget (OMB Cost Principles). Initially, these cost principles were set forth in OMB Circular A-87 (Cost Principles for State, Local, and Indian Tribal Governments).[2] In December 2016, Treasury updated its contracts to instead adopt OMB's uniform cost principles for Federal awards, the most up-to-date requirements applicable to state and local governments, non-profit organizations, and other non-Federal recipients of Federal funds.[3]

As a basic condition of allowability, the OMB Cost Principles have always required that administrative expenses be necessary for the performance of the HHF contract. Other basic conditions include being reasonable (in nature and amount), allocable to the HHF contract, and adequately documented. The OMB Cost Principles also provide detailed requirements governing the allowability of specific types of expenses. For example, the cost principles recognize that many forms of employee compensation may be allowable—*e.g.*, salaries, wages, health insurance and other benefits, incentive compensation, and severance pay—but only under certain circumstances. These principles also prohibit certain types of expenses which are clearly inappropriate for the Federal government to bear—*e.g.*, tickets to shows, sporting events, or other forms of personal entertainment.

II. Treasury Monitors HFAs' Compliance With HHF Program Requirements.

Treasury evaluates compliance with HHF program requirements—including, but not limited to, the OMB Cost Principles—through regular, on-site compliance reviews. These include reviews of administrative expenses and other program activity on a sample basis. For each sampled administrative expense, Treasury evaluates whether the expense is consistent with the approved budget, supported by an invoice or other documentation, and allocable to HHF, among other things. Last year, Treasury enhanced its testing of administrative expenses in two ways. First, we increased the sample size—*i.e.*, the number of transactions selected for testing—for types of expenses that present a higher risk of non-compliance. Second, we increased our sampling of small-dollar transactions.

States are required to implement internal controls to help ensure that HHF programs are run effectively, efficiently, and in compliance with Treasury's contract. Examples of controls related to administrative expenses include (i) maintaining written policies that describe requirements applicable to administrative expenses, (ii) increased scrutiny of high-dollar transactions or types of expenses which present elevated risks of non-compliance, and (iii) routine reviews of administrative expense payments by internal auditors or quality assurance teams. States' internal controls are evaluated by Treasury during its on-site reviews and independently verified on an annual basis. Treasury has observed that, with these controls in place, states have identified improper expenditures and obtained repayment as needed.

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[1] P. 1

[2] These principles were set forth in 2 C.F.R. Part 225 and can be viewed at: https://www.gpo.gov/fdsys/pkg/CFR-2012-title2-vol1/pdf/CFR-2012-title2-vol1-part225.pdf.

[3] 2 C.F.R. §§ 200.400-475.

III. Treasury Recovers Funds Where Appropriate and Takes Other Actions to Enforce the Terms of its Contracts with HFAs.

Treasury requires HFAs to repay HHF when Treasury identifies improper expenditures. This has included, for example: bonuses and other compensation which did not meet applicable requirements; non-business related travel and entertainment; food, beverages, gifts, and other items for employees' personal use; legal expenses not required for the proper administration of HHF; charges not related to HHF; and charges not supported by documentation. Earlier this year, Treasury required states to repay $33,592 to HHF for improper expenditures that SIGTARP later identified in the Draft.

Treasury also requires that HFAs take other corrective actions. For example, where Treasury identifies a potentially systemic error, Treasury requires the HFA to conduct a look-back analysis to ascertain the full impact of the error, and revise its procedures as needed to ensure that the error does not reoccur in the future. In addition, Treasury requires states to establish or improve internal controls around key functions when Treasury identifies a deficiency.

Furthermore, Treasury has worked diligently to analyze expenditures questioned by SIGTARP in the past, and recover funds that we determined were improperly spent. For example, when Treasury received SIGTARP's recommendations regarding its 2016 audit of administrative expenses in the Nevada HHF program, we undertook a thorough analysis that led to HHF recovering more than $80,000. For the reasons set forth in our letter to you on January 19, 2017, Treasury determined that recovery of certain other expenditures was not warranted.[4] We will undertake a similarly thorough analysis with respect to the recommendations in the Draft.

* * *

To facilitate our analysis, we have requested under separate cover that SIGTARP provide us with more specific information for certain of the expenses questioned in the Draft. We note that the Draft provides transaction-level detail for some expenses (*e.g.*, the purchase of a water bottle for $1.81) but describes other expenses on an aggregate basis only (*e.g.*, $330,575 in parking subsidies for employees at one HFA). The expenses referred to in the Draft also span all 19 HFAs, and appear to date back to the outset of the program. We look forward to receiving these important details from you, so that we can move quickly to review the remaining expenses and recover any taxpayer funds that have been improperly spent.

Even as the TARP program nears its end, we remain committed to taking appropriate actions to improve program performance and protect the interests of taxpayers. We look forward to continuing to work with you as we wind down TARP.

Sincerely,

Lorenzo Rasetti

Lorenzo Rasetti
Chief Financial Officer
Office of Financial Stability

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[4] https://www.treasury.gov/initiatives/financial-stability/about-tarp/Pages/Oversight-and-Accountability.aspx.