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

[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