

May 12, 2016

TO: State Directors
Rural Development

ATTN: Program Directors
Single Family Housing

FROM: Tony Hernandez /s/ ***Tony Hernandez***
Administrator
Housing and Community Facilities Programs

SUBJECT: Fiscal Year 2015 Management Control Review
Section 504 Loan and Grant Program

PURPOSE:

The purpose of this Unnumbered Letter is to address the weaknesses identified in the Fiscal Year (FY) 2015 Management Control Review (MCR) of the Section 504 Loan and Grant Program. The objective of the MCR was to evaluate the program's effectiveness, identify deficiencies and weaknesses, and make recommendations for program improvements.

BACKGROUND:

The basis for performing the MCR for the Section 504 Loan and Grant Program was to assess the risk or vulnerability of inadequate controls, determine if adequate control measures and/or objectives have been established, and determine if these controls are functioning effectively to achieve the overall goals of the program. The MCR was utilized to identify strengths and concerns in the Section 504 program nationwide, and to identify corrective actions and make recommendations for program improvement. Both National and State Office program delivery were reviewed and evaluated.

EXPIRATION DATE:
February 28, 2017

FILING INSTRUCTIONS
Housing Programs

The review included one state on-site review as well as loan and grant docket reviews from nine states representing a cross section of the program across the country. Three control objectives were utilized to evaluate the program:

1. To ensure that applicant eligibility, income verification and credit requirements are met.
2. To ensure that property eligibility, ownership requirements and construction standards are met.
3. To ensure funds are used for authorized eligible loan and grant purposes and are fully disbursed within a timely manner.

The full final report can be found at <http://teamrd.usda.gov/rd/daom/cfo/fmd/mc.html>.

FINDINGS AND RECOMENDATIONS:

The MCR revealed several weaknesses that must be addressed in order to strengthen the program and reduce risk and the potential for losses to the government. A discussion of each follows:

Documentation

Attachment 12-C, “504 Single Family Housing Loan and Grant Checklist” was often found to be the only source of documentation in case files. Although the checklist is required and is important for uniformity purposes, it does not replace the running record. There was found to be an overall lack of sufficient documentation and running records were incomplete or nonexistent. It is imperative to keep a running record with a detailed account of application processing, dates and photographs for verification.

The loan originator must thoroughly document the Section 504 Loan and Grant case file and follow guidance provided in RD Instruction 2033-A, which provides the policies, procedures and methods for maintaining and managing Rural Development records. Maintaining accurate documentation adds credibility to internal and external audits, compliance regulations, statements made by the applicant/borrowers, and supports eligibility determinations.

Credit Reports

During the review, several instances were found where credit reports were ordered for grant recipients. Handbook-1-3550, Chapter 12 states, “The Loan Originator need not evaluate the credit history of grant applicants. Credit reports *will not* (emphasis added) be ordered for 504 grant applicants.” However, for loans, applicants must have a credit history that indicates a reasonable ability and willingness to meet debt obligations.

Regardless of the size of the loan, the Loan Originator must check both the In-file Credit Report and HUD's Credit Alert Verification Reporting System (CAIVRS). Credit reports are required with applications for loans of \$7,500 or greater. However, Section 504 loan credit requirements may be less stringent than Section 502 loans.

Repair Estimates

For several cases, no photographs were taken of the property. Also, there were cases without three contractor bids or an explanation for why three bids were not obtained. The Loan Originator must visit the property within 30 days of eligibility determination to assess what repairs are needed. Photographs should also be taken of needed repairs during this visit. The applicant will then use the repair list to solicit bids from contractors. Handbook-1-3550 states, "The applicant will be provided with a detailed set of specifications, which will be utilized to solicit 3 bids when feasible." If obtaining three bids is not feasible for the area, document and justify the reason in the case file.

Grant Agreement

HB-1-3550, Chapter 12, paragraph 12.9, states, "Before any grant funds are disbursed, the recipient must sign Form 3550-24, Grant Agreement." However, there was a case when the grant agreement was not signed. The agreement states that if a home repaired with a Section 504 grant is sold within three years of grant approval, the full amount of the grant must be repaid. The original form is filed in a locked file cabinet, with a copy to the case file and a copy provided to the recipient.

Verification of Prior Grant Assistance

The Loan Originator must verify the existence of prior grant assistance through either the DLOS system, Hyperion reports, or a list of prior recipients kept in the office operational files. In some instances, there was no evidence of verification of prior grant assistance. HB-1-3550, Chapter 12, paragraph 12.9, requires that the Loan Originator document any previous grants received by an applicant to ensure that applicants do not receive more than the lifetime maximum allowable assistance of \$7,500. The list should include (1) the grantee's name, address, and case number; (2) the amount of the grant; and (3) the date the grant was approved.

Questions regarding this memorandum should be directed to Andrea Birmingham, or Carolyn Bell, of the Single Family Housing Direct Loan Division, at (202) 720-1474.