

CALIFORNIA DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT

Review Report

STATE RENTAL ASSISTANCE PROGRAM

Compliance and Oversight

March 1, 2021, through June 30, 2021

Applications and Payments

April 14, 2021, through December 31, 2021



BETTY T. YEE
California State Controller

August 2022



BETTY T. YEE
California State Controller

August 16, 2022

Gustavo Velasquez, Director
California Department of Housing and Community Development
2020 West El Camino Avenue
Sacramento, CA 95833

Dear Mr. Velasquez:

The State Controller's Office conducted a review of the California Department of Housing and Community Development's oversight of its State Rental Assistance Program for the period of March 1, 2021, through June 30, 2021.

If you have any questions, please contact Michael Reeves, Assistant Chief, Field Audits Branch, Division of Audits, by telephone at (916) 323-5849, or by email at mreeves@sco.ca.gov.

Sincerely,

Original signed by

KIMBERLY TARVIN, CPA
Chief, Division of Audits

KT/lis

cc: Janell Bonilla, Acting Deputy Director, Administration and Management
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Review Report

Summary

The California Department of Housing and Community Development (HCD) contracted with the State Controller's Office (SCO) to review HCD's oversight of the State Rental Assistance Program (SRAP) for the period of March 1, 2021, through June 30, 2021. HCD also contracted with SCO to review SRAP applications and payments beginning with the initial payments dated April 14, 2021, through October 31, 2022. This report incorporates results of the SRAP application and payment review for the period of April 14, 2021, through December 31, 2021. HCD requested that we conduct these reviews to identify internal control weaknesses and process improvements to strengthen HCD's oversight of the SRAP.

The SRAP provides rent relief to California landlords and renters who have faced financial hardships due to the COVID-19 pandemic. The SRAP is administered by HCD and local agencies and has provided approximately \$4.27 billion in rental assistance to vulnerable Californians. Local agency jurisdictions were able to choose from three allocation and administration processors, which are categorized as Options A, B, and C. Option A jurisdictions elected to have HCD administer their share of SRAP funds; Option B jurisdictions elected to self-administer their SRAP funds; and Option C jurisdictions administer their direct SRAP allocations and elected to have HCD administer their proportionate SRAP share.

The results of our review of HCD's oversight of the SRAP, and of the SRAP applications and payments, are as follows:

- HCD's vendor approved 488 potentially fraudulent SRAP applications totaling \$18.1 million during the period of July 1, 2021, through December 31, 2021. A total of \$7 million for 186 of the 488 applications has been disbursed. An additional \$11.1 million could also have been disbursed for the remaining 302 applications had we not identified them as potentially fraudulent.

Approximately \$109,000 of these disbursed funds is either in the process of being voided, or has not cleared the bank.

HCD agrees with SCO that the remaining \$6.9 million in disbursed funds represents potentially fraudulent payments. HCD indicated that once its vendor has exhausted its efforts in recapturing the remaining \$6.9 million, HCD will attempt to recover the disbursed funds by using intercept programs (such as the Franchise Tax Board's Interagency Intercept Collection Program, which collects money from state tax refunds, lottery winnings, and unclaimed property) and by bringing cases to the California Attorney General. However, these methods may not allow for recovery of the disbursed funds if the recipients used fictitious information.

- HCD's vendor lacked adequate controls over the application review process, resulting in overpayments and underpayments.
- HCD's vendor did not consistently request death match verifications before approving applications for payment. However, our review did not identify any improper payments as a result of not consistently performing this procedure.

- HCD’s vendor lacked adequate controls over the application review process for Option C jurisdictions to prevent improper payments.
- HCD’s vendor modified and processed pay files without HCD’s approval of the adjustments.
- HCD should continue current monitoring procedures and increase on-site monitoring of Option B jurisdictions based on a risk assessment to ensure compliance with executed standard agreements and federal program guidelines.
- HCD did not ensure that its vendor implemented corrective actions for all errors and issues identified by SCO and HCD.
- HCD did not establish adequate control procedures regarding landlord and tenant documentation requirements necessary to mitigate the risk of fraud and misuse of funds.

Background

The federal Emergency Rental Assistance Program provides funding directly to states, U.S. territories, and local governments to assist households that are unable to pay rent due to the COVID-19 pandemic. Up to \$25 billion became available under the federal Consolidated Appropriations Act of 2021, enacted on December 27, 2020. California initially received approximately \$2.6 billion in rental assistance funds; the State administered \$1.5 billion, and the remaining \$1.1 billion was allocated directly to local jurisdictions with populations over 200,000. As of the date of this report, the SRAP has paid out approximately \$4.27 billion in rental assistance payments.

On January 29, 2021, Senate Bill 91 (Chapter 2, Statutes of 2021), which amended the Budget Act of 2020 to fund the SRAP, was enacted. The primary objective of the SRAP is to help eligible households pay rent and utilities costs. The highest priority is given to rental arrears incurred between April 1, 2020, and March 31, 2021; jurisdictions that have administered payments for these rental arrears may provide assistance for current and prospective rent. SB 91 defines *prospective* rent as rent due for April 2021 and thereafter.

SB 91 appropriates \$1.5 billion from the Federal Trust Fund to HCD for purposes of implementing the SRAP. SB 91 also extends the eviction moratorium provisions established by Assembly Bill 3088 (Chapter 37, Statutes of 2020), until June 30, 2021. SB 91 prevents the eviction of tenants who pay at least 25% of their owed rent.

SB 91 specifies the amount of assistance that applicants can receive and the assistance period. For April 2020 through March 2021 (the arrears period), assistance for either 80% of the total rent in arrears if paid directly to landlords, or 25% of the total rent in arrears if landlords refused to participate in the program, was available to eligible tenants. For April 2021 and after (the prospective period), assistance for 25% of the prospective monthly rental amount—whether paid to landlords or tenants—is available to eligible tenants.

On June 28, 2021, AB 832 (Chapter 27, Statutes of 2021) was enacted. AB 832 increases the compensation amount to 100% for rent in arrears and prospective rent, and allows direct payment to tenants in situations where landlords refuse to participate in the program.

Jurisdictions were able to choose from three allocation and administration processes, which are categorized into Options A, B, and C:

- Option A jurisdictions received direct allocations of funds (direct federal allocation) from the U.S. Department of the Treasury (U.S. Treasury), but elected to have HCD administer these funds. These jurisdictions also elected to have HCD administer their shares of State Rental Assistance Funds (proportionate SRAP share).
- Option B jurisdictions elected to administer their direct federal allocations. These jurisdictions elected to receive their proportionate SRAP shares as block grants, which they will also administer.
- Option C jurisdictions elected to administer their direct federal allocations, but elected to have HCD administer their proportionate SRAP shares.

HCD contracted with a vendor to implement the SRAP. The vendor processes applications with the Neighborly Software (Neighborly) system, and distributes SRAP funds for Option A and C jurisdictions. HCD and its vendor began distributing SRAP funds on April 14, 2021.

Review Authority

We conducted this review at the request of HCD, in accordance with Interagency Agreement Number 20-50-021 between SCO and HCD.

In addition, Government Code (GC) section 12410 states, in part:

The Controller shall superintend the fiscal concerns of the state. The Controller shall audit all claims against the state, and may audit the disbursement of any state money, for correctness, legality, and for sufficient provisions of law for payment.

Objectives, Scope, and Methodology

Our review objectives were to determine whether:

- SRAP applications and documentation complied with the federal program requirements established by SB 91 and the federal cognizant agency, the U.S. Treasury; and
- HCD established adequate oversight of the SRAP.

The review period was March 1, 2021, through June 30, 2021. This report also includes results of our review of SRAP applications and payments from April 14, 2021, through December 31, 2021.

To achieve our review objectives, we completed the following:

- We conducted inquiries and interviews about the SRAP payment process with knowledgeable staff members of HCD and HCD's vendor to gain an understanding of the payment transaction flow and oversight of the payment process.

- We reviewed California SB 91 and the federal Consolidated Appropriations Act of 2021.
- We reviewed HCD and the vendor's documented procedures, which included:
 - HCD's *COVID-19 Rent Relief Program Administrative Plan* (June 29, 2021);
 - Sample landlord and tenant intake applications from Neighborly;
 - Case Manager (CM) Reviewer Checklists and Quality Assurance/Quality Control (QA/QC) Checklists;
 - *Neighborly Application to Payment Workflow*;
 - *COVID-19 Rent Relief Case Manager Standard Operating Procedures* (March 27, 2021); and
 - *COVID-19 Rent Relief Quality Assurance/Quality Control Standard Operating Procedures* (April 29, 2021).
- We attended SRAP meetings related to payment and vendor oversight.
- For all 7,561 applications submitted by the vendor to HCD from March 1, 2021, through June 30, 2021, we verified whether death match verification was requested before payment.
- We performed random and targeted selections of applications for testing to determine whether approved applications complied with all statutory requirements, and to verify that payments were accurate and proper. We tested the following payments from these weekly pay files:
 - April 26, 2021 – 102 of 142 payments (\$875,512 of \$1,253,447);
 - May 3, 2021 – 20 of 290 payments (\$129,346 of \$2,452,108);
 - May 10, 2021 – 86 of 457 payments (\$1,098,674 of \$5,605,743);
 - May 17, 2021 – 120 of 716 payments (\$1,754,556 of \$9,678,580);
 - May 24, 2021 – 106 of 811 payments (\$1,342,563 of \$9,823,690);
 - June 1, 2021 – 88 of 573 payments (\$920,714 of \$5,711,824);
 - June 7, 2021 – 134 of 1,088 payments (\$481,156 of \$3,183,377);
 - June 14, 2021 – 113 of 1,970 payments (\$616,222 of \$11,380,582);
 - June 21, 2021 – 133 of 1,803 payments (\$749,893 of \$11,415,970); and
 - June 28, 2021 – 134 of 2,061 payments (\$645,066 of \$11,674,776).

We reported to HCD the results of our testing, including any observations and errors, for each weekly pay file reviewed.

- We analyzed transactions from the pay files to identify variances between approved payment amounts and Neighborly information.
- We reviewed the responses from HCD's vendor to issues that we noted during our review to determine whether corrective actions had reportedly been taken, and whether HCD verified that corrective actions had been taken.

- In accordance with the interagency agreement between SCO and HCD, we judgmentally sampled additional applications for the period of July 1, 2021, through December 31, 2021. During this period, we reviewed weekly disbursement files to identify anomalies that could be precursors to potential fraud. Because of their sensitive nature, these issues are not discussed in this report; however, we have discussed the issues with HCD management.

Conclusion

Our review of SRAP applications and payments for the period of April 14, 2021, through December 31, 2021, found the following:

- HCD's vendor approved 488 potentially fraudulent SRAP applications totaling \$18.1 million during the period of July 1, 2021, through December 31, 2021. A total of \$7 million for 186 of the 488 applications has been disbursed. An additional \$11.1 million could also have been disbursed for the remaining 302 applications had we not identified them as potentially fraudulent.

Approximately \$109,000 of these disbursed funds is either in the process of being voided, or has not cleared the bank.

HCD agrees with SCO that the remaining \$6.9 million in disbursed funds represents potentially fraudulent payments. HCD indicated that once its vendor has exhausted its efforts in recapturing the remaining \$6.9 million, HCD will attempt to recover the disbursed funds by using intercept programs (such as the Franchise Tax Board's Interagency Intercept Collection Program, which collects money from state tax refunds, lottery winnings, and unclaimed property) and by bringing cases to the California Attorney General. However, these methods may not allow for recovery of the disbursed funds if the recipients used fictitious information; see Finding 1.

Our review of HCD's compliance and oversight of the SRAP program for the period of March 1, 2021, through June 30, 2021, found the following:

- HCD's vendor lacked adequate controls over the application review process, resulting in overpayments and underpayments; see Finding 2.
- HCD's vendor did not consistently request death match verifications before approving applications for payment. However, our review did not identify any improper payments as a result of not consistently performing this procedure; see Finding 3.
- HCD's vendor lacked adequate controls over the application review process for Option C jurisdictions to prevent improper payments; see Finding 4.
- HCD's vendor modified and processed pay files without HCD's approval of the adjustments; see Finding 5.
- HCD should continue current monitoring procedures and increase on-site monitoring of Option B jurisdictions based on a risk assessment to ensure compliance with executed standard agreements and federal program guidelines; see Finding 6.

- HCD did not ensure that its vendor implemented corrective actions for all errors and issues identified by SCO and HCD; see Finding 7.
- HCD did not establish adequate control procedures regarding landlord and tenant documentation requirements necessary to mitigate the risk of fraud and misuse of funds; see Finding 8.

Views of Responsible Officials

We issued a draft review report on June 13, 2022. HCD representatives responded by letter dated July 15, 2022, partially agreeing with Findings 1, 2, and 8; and disagreeing with Findings 3 through 7. HCD also indicated that it will implement our recommendations where appropriate, and has taken some actions, which we did not validate, to address the noted deficiencies. This final review report includes HCD's response as an attachment.

Restricted Use

This report is solely for the information and use of HCD and SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of this review report, which is a matter of public record and is available on the SCO website at www.sco.ca.gov.

Original signed by

KIMBERLY TARVIN, CPA
Chief, Division of Audits

August 16, 2022

Findings and Recommendations

FINDING 1— Potential fraud identified

We identified 488 potentially fraudulent applications totaling approximately \$18.1 million during our review of SRAP applications that were target selected during the period of July 1, 2021, through December 31, 2021. HCD's vendor disbursed approximately \$7 million for 186 of the 488 applications between May 28, 2021, and December 31, 2021. An additional \$11.1 million could also have been disbursed for the remaining 302 applications had we not identified them as potentially fraudulent.

Approximately \$109,000 of these disbursed funds is either in the process of being voided, or has not cleared the bank.

HCD agrees with SCO that the remaining \$6.9 million in disbursed funds represents potentially fraudulent payments. HCD indicated that once its vendor has exhausted its efforts in recapturing the remaining \$6.9 million, HCD will attempt to recover the disbursed funds by using intercept programs (such as the Franchise Tax Board's Interagency Intercept Collection Program, which collects money from state tax refunds, lottery winnings, and unclaimed property) and by bringing cases to the California Attorney General. However, these methods may not allow for recovery of the disbursed funds if the recipients used fictitious information.

As of December 31, 2021, a total of approximately \$1.5 billion in SRAP funds had been disbursed. If the vendor application review process is not enhanced, HCD will continue to be at risk of making improper payments to applicants who submitted potentially fraudulent applications. HCD's vendor can strengthen its application and supporting documentation review processes as follows:

Duplicate landlord and case IDs

The vendor's CM checklist includes a procedure to check for name and address duplications within Neighborly to prevent processing and payment of duplicate applications and duplicate landlord case IDs. However, this procedure was not adequately performed. Our application review found indications of potential fraud. For example, we identified a significant number of tenant applications associated with the same apartment complex that were also associated with multiple landlord IDs. Additionally, some of the payments to the multiple landlord case IDs were paid via check and others were paid via Automated Clearing House.

Potentially fraudulent supporting documentation

Based on our review of the documentation retained in the vendor's files at the time that applications were approved, the vendor did not identify supporting documentation that appeared to be illegitimate, altered, or inconsistent with legitimate forms of identification. Although some potentially fraudulent documents would have been identified as such only upon more careful inspection, in some cases there were clear and visible signs that documents had been altered—which HCD's vendor should have identified upon proper inspection. Some of the potentially fraudulent

transactions might have been identified if program documentation requirements had been more stringent, if applicants had been required to produce additional supporting documentation, or if additional third party verifications had been performed by HCD or its vendor, as recommended in Finding 8.

Title 2, Code of Federal Regulations (2 CFR), part 200.303 states:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework,” issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). . . .
- (c) Evaluate and monitor the non-Federal entity’s compliance with statutes, regulations, and the terms and conditions of Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings

Recommendation

We recommend that HCD:

- Ensure that its vendor verifies that there are no duplicate landlord case IDs or tenant case IDs for the same address before processing applications;
- Consolidate landlord case IDs for legitimate applications to ensure that payment is made to the appropriate landlord;
- Instruct its vendor to provide additional fraud training to staff. Specifically, provide training on how to recognize potentially fraudulent and altered documents;
- Require landlord applications to provide proof of ownership documentation such as a property tax bill, homeowner’s insurance bill, or deed of trust;
- Verify at least one of the documents provided by the tenant or landlord for questionable applications and applications that request large dollar amounts of assistance. Specifically, HCD should use third-party verification to verify the legitimacy of questionable forms of ID, utility bills, and tax forms; and to verify the legitimacy of property ownership documentation; and
- Investigate the potentially fraudulent applications identified by SCO; deny the fraudulent applications confirmed; and recover funds that were paid to fraudulent applicants.

HCD's Response

HCD partially agrees with this finding for the initial cases identified; however, as noted above, HCD implemented many process improvements since the initial SCO review was conducted. HCD will continue to identify, where applicable, recommendations that can be taken into consideration with the limited time left in the program as well as in future emergency housing initiatives.

Specific findings of the review are addressed below:

Duplicate landlord and case IDs

The Program is focused on preventing multiple/duplicate tenant applications per property (address and unit) that could result in duplicate benefits being paid. Within this focus and the daily operation, it is common for a large landlord to have multiple applications because larger landlords may have multiple properties and multiple management companies. Benefits are approved and awarded based on a qualified tenant, not a qualified landlord.

The program does track instances of multiple landlord applications as the review notes, but this condition alone is not an issue since awards are based solely on tenant eligibility. Only combined with other factors do instances of multiple landlord applications then begin to indicate potential fraud.

Potentially fraudulent supporting documentation

For the period between 7/1/2021 thru 12/31/2021, ERAP¹ approved 201,000 tenant applications. The identified 488 “potentially” fraudulent applications translate to 0.2% of all approved ERAP applications processed during this period. With over \$1.5 billion disbursed, the \$7 million in funds disbursed to potentially fraudulent applications represents 0.4% of all funds disbursed during the same period. The Program has worked closely with SCO and other state and federal partners to minimize the incidence as well as undertaking efforts to recapture any funding that has been disbursed.

Documentation requirements and staff training have continued to evolve throughout the duration of the program. As strongly recommended through program guidance provided by the U.S. Treasury, the program provides various alternative documentation options for applicants to submit, depending on their circumstances. Documentation submitted, will therefore vary. HCD and its vendor have continuously sought to ensure staff are equipped to identify potentially fraudulent documentation. This is, in part, the reason HCD contracted with the SCO to help provide additional third-party verification. The strong partnerships between SCO and HCD, as well as HCD and the third-party vendor, allowed program staff to continue focusing on disbursing funds while broader programmatic improvements were initiated.

¹The Emergency Rental Assistance Program (ERAP) is also referred to as the State Rental Assistance Program (SRAP).

Recommendations

In regard to the multiple recommendations, we have a few comments, while acknowledging we do not disagree and will proactively implement them where appropriate. Our comments are as follows:

- As previously noted, HCD has seen instances where large landlords (or property management companies with multiple agents) manage multiple properties, therefore creating multiple landlord files. As stated in the previous response, multiple landlord case files are not unusual. The Program focus is on duplicate tenant case files and preventing multiple tenant applications for the same property.
- The vendor provides fraud training to all case managers in their employee orientation. There are also stand-down presentations for fraud as well as recorded fraud trainings. Additionally, the vendor has a dedicated and seasoned team of resources in place to undertake fraud review. HCD can provide a sample of the specific onboarding fraud training, presentations as well as the recorded training module. It is also important to note that the vendor has extensive experience in delivering large programs and projects nationally and is accustomed to working with federal funds. The vendor's core service is accounting and has served as the prime contractor for disaster recovery and direct service programs.

In response to earlier SCO recommendations, HCD implemented internal control reviews, whereby HCD Internal Control Auditors, select and review approved applications prior to payment disbursement. Performed weekly, applications are reviewed for documentation completeness, eligibility, assistance amount approved, and checked for landlord property ownership where applicable. HCD Internal Control Auditors also conducted data analysis on specific application and assistance attribute to locate potentially fraudulent cases for additional review.

- In September 2021, the vendor implemented a policy to address high dollar rents. This policy limits the monthly rent assistance available on any given property to not exceed a certain percentage above HUD's Fair Market Rent (FMR).
- In December 2021, the vendor instituted the requirement that participating landlords must provide third-party documentation supporting proof of property ownership. In February 2022 the vendor incorporated a business subscription with the ability to verify public records, thereby providing the vendor and their fraud unit the ability to research various public records.
- HCD has reviewed the potential fraudulent applications identified by SCO, and those suspected applications have been denied and a recapture has been initiated. HCD is developing a procedure working with the California State Franchise Tax Board to intercept funds not recaptured/repaid by a fraudulent applicant as well as partnering with law enforcement.

SCO Comment

Our finding and recommendation remain unchanged. SCO recognizes that HCD implemented corrective actions after our review period ending June 30, 2021, and commends HCD's commitment to reducing fraud and errors in payment files. We also recognize that HCD has taken actions to recover potentially fraudulent payments.

For clarification, we identified the majority of potential fraud based on irregular personal identification documentation contained within the applicant files, and not related to multiple landlord applications. Tracking and associating applications with the same landlord *would* assist HCD in identifying fraud, especially when a landlord initiates an application on behalf of multiple tenants or when irregularities are identified with a particular landlord.

HCD stated that the 488 potentially fraudulent applications identified in our limited review represent 0.2% of the 201,000 approved SRAP applications during the period of July 1, 2021, through December 31, 2021. Our review included only a small sample of the 201,000 applications processed during that period, and we did not estimate the actual percentage of potentially fraudulent transactions within the 201,000 applications processed.

**FINDING 2—
Verification
procedures not
consistently or
effectively
performed resulting
in overpayments and
underpayments**

HCD's vendor did not consistently or effectively perform the required application and payment review procedures, resulting in overpayments of \$287,416 and underpayments of \$97,823. The internal control procedures were developed for CM and QA/QC staff to ensure that payments to program recipients are accurate and comply with program requirements. If HCD's vendor does not consistently and effectively perform the required internal control procedures, HCD is at risk of approving additional improper payments.

HCD's vendor processed 9,911 transactions totaling \$72,180,097 for payment between April 26, 2021, and June 28, 2021. We randomly selected and tested 1,007 (or 10.2%) of 9,911 transactions from 10 pay files totaling \$8,555,647 (or 11.9% of the total \$72,180,097). Of the 1,007 randomly selected transactions, 165 were overpayments, totaling approximately \$287,416, and 144 were underpayments, totaling approximately \$97,823.

The overpayments and underpayments occurred because the vendor's CMs and QA/QC staff did not perform all of the internal control procedures included in the checklists, or completed the procedures inaccurately. We tested 1,007 transactions, and noted that 967 CM checklists and 992 QA/QC checklists were incomplete; we also noted that 309 transactions were inaccurately calculated by the vendor's CMs and subsequently approved by QA/QC staff. The overpayments and underpayments could have been prevented if all of the internal control procedures in the checklists had been performed as designed (see the table below). A completed checklist indicates that all internal control procedures were performed before applications were approved for payment. Checklists in Neighborly were revised during the review period, which may have resulted in some incomplete checklists. However, without documentation to support that all control procedures were completed, the vendor cannot demonstrate that internal control procedures were performed.

The table below summarizes the number of uncompleted or inaccurately performed procedures, resulting in an overpayment or underpayment.

Internal Control Procedure in Checklists	Number of Times Procedure Failed, Resulting in Erroneous Payment
Verify that lease and rent amounts are eligible and accurate	199
Verify that utilities are eligible per rental agreement	34
Verify that late fees were not included	46
Verify that there is no duplication of benefits (for Option C jurisdictions: Also verify eligibility for arrears period assistance under state program)	24
Verify that late fees were not included, and verify all income documentation provided (two controls failed)	1
Verify that late fees were not included, and verify that utilities are eligible per rental agreement (two controls failed)	3
Verify that lease and rent amounts are eligible, and verify all income documentation provided (two controls failed)	2

Overpayments and underpayments occurred because CMs:

- Used incorrect ending balances on rent ledgers to calculate assistance;
- Included late fees in rental assistance amounts;
- Did not approve utility amounts billed by landlords;
- Approved assistance for prospective rent when it was not requested;
- Included rental debt prior to April 1, 2020, in calculations;
- Did not verify that Option C applicants had applied through the correct program; and
- Did not determine whether prior assistance had been received and was reflected on rent ledgers.

GC sections 13400 through 13407 require state agencies to establish and maintain systems of internal control, as fraud and errors are more likely to occur from a lack of effective systems of internal control when active monitoring measures are not maintained to ensure that controls are functioning properly.

In addition, 2 CFR part 200.303 states:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal

Control Integrated Framework,” issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). . . .

- (c) Evaluate and monitor the non-Federal entity’s compliance with statutes, regulations, and the terms and conditions of Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings. . . .

Recommendation

We recommend that HCD:

- Ensure that the vendor’s CMs and QA/QC staff properly complete checklists before approving applications for payment;
- Recover overpayments made to applicants, and properly compensate applicants that were underpaid; and
- Attend vendor training sessions for CMs and/or QA/QC staff to ensure that such training is in accordance with HCD guidance.

HCD’s Response

It is important to note that HCD was in the process, and has since finalized, the recommended improvements provided at the time of SCO’s review.

However, portions of the findings stated in the SCO review require clarification:

- The basis for this finding stems from the requirement provided in Senate Bill (SB) 91, effective January 29, 2021, originally limiting the program to provide partial compensation for both direct to landlord and direct to tenant payments. This statutory requirement was subsequently amended following the passage of Assembly Bill (AB) 832, effective June 28, 2021, authorizing the program to provide compensation for 100 percent of rent owed to be paid. Following the enactment of AB 832, the vendor was able to go back and pay the remaining balance of unpaid rent (top-off) attributed to the previous partial compensation requirements the program was required to follow under state law. Any overpayments from the early months were taken into consideration in the top-off payment by discounting the top-off disbursement. HCD can provide the total count of applications and amounts paid through this process.
- This is a datapoint specific to the first three months of the program. As such, the total number of cases reviewed represents less than 3% of volume to date.

SCO Comment

Our finding and recommendation remain unchanged. We appreciate HCD’s commitment to implementing our recommendations and recognize that HCD and its vendor may have implemented improvements to these processes after June 30, 2021.

For clarity, the basis of this finding does not stem from the enactment of AB 832. This finding is based on our review of a sample of 1,007 transactions whereby we determined that, for the majority of transactions reviewed, verification procedures and review checklists were either not performed, partially performed, or performed inaccurately. The enactment of AB 832, chaptered on June 28, 2021 (two days before the end of our review period), did not change the application verification procedures or the internal controls that should have been performed and documented by HCD's vendor, except for HCD's requirement of calculating the percentage of payment. We believe that the underpayments and overpayments processed during the review period would have been reduced had HCD's vendor performed the required verification procedures and internal control processes.

**FINDING 3—
Death match
verification not
consistently requested
before payment
approved**

HCD's vendor did not consistently perform the internal control procedure of requesting a death match verification for each application before approving for payment. In the pay files for April 19, 2021, through June 28, 2021, we identified 1,836 (or 24%) of 7,561 applications approved for payment by HCD for which the vendor did not request death match verifications prior to approval. The purpose of this internal control procedure is to screen out potentially fraudulent applications for further review prior to eligibility determination. If these internal control deficiencies are not mitigated, HCD is at risk of making payments to individuals who submitted fraudulent applications.

The internal control procedure established at the beginning of the SRAP requires the vendor to submit a list of applicant names and birth dates to SCO to be verified in a database comprising the names and birth dates of deceased individuals prior to issuing payment. In addition, the vendor's QA/QC checklist includes a procedure to verify the applicant information against the results of the death match verification prior to payment. Prior to June 1, 2021, SCO was provided with 1,895 applicant names for death match verification. SCO received an additional 91,338 applicant names on June 1, 2021.

During the review period, we informed HCD of death match verifications not being requested prior to approval for payment. In response, on July 12, 2021, HCD revised the procedure requiring the vendor to submit a list of applications for the death match verification every Friday. As of the date of this report, HCD has fully implemented this procedure. However, we continue to find applications that were approved for payment without death match verifications having been requested prior to approval.

HCD's *COVID-19 Rent Relief Program Administrative Plan*, section 16.3, "Audit of RAP Payments," states:

... HCD also establish[ed] the following data repositories for case management to screen out potentially fraudulent applications for further review prior to eligibility determination. These repositories are. . .

2. State Controller's Office Death File: Matching applicant information (name and DOB) to individuals reported to be deceased to detect potentially fraudulent applications. . . .

During our review of applications and supporting documentation, we found that the vendor's controls did not operate effectively. We noted instances in which QA/QC checklists indicated that applicant information had been verified against death records when this could not have occurred, as no death match verification had been requested. Furthermore, we noted instances in which applications were processed for payment although the related checklists indicated that death match verification had not been performed.

We did not identify any applicant names that matched death records during our review. However, if applicant names are not matched to death records for every application, HCD is at risk of making payments to individuals who submitted fraudulent applications.

GC sections 13400 through 13407 require state agencies to establish and maintain systems of internal control, as fraud and errors are more likely to occur from a lack of effective systems of internal control when active monitoring measures are not maintained to ensure that controls are functioning properly.

In addition, 2 CFR part 200.303 states:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework," issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). . . .
- (c) Evaluate and monitor the non-Federal entity's compliance with statutes, regulations, and the terms and conditions of Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings. . . .

Recommendation

We recommend that HCD establish internal control policies and procedures to monitor and confirm that its vendor compares all SRAP applications to death records before issuing payment.

HCD's Response

HCD disagrees with this finding, as the SCO review did not identify any payment disbursed to an application submitted by a deceased person. Since program inception, the program has had a death match verification process and internal controls in place. This process is utilized in the review of all files before payment is issued. The vendor performs procedures developed by HCD in collaboration with SCO, including requiring the case manager to verify applicant identification against death roll records obtained by a third-party vendor.

SCO Comment

Our finding and recommendation remain unchanged. We agree that HCD established procedures for death match verification at the program's inception. However, our review identified instances in which death match procedures were not performed for all applications before they were approved for payment.

FINDING 4— Inadequate controls over Option C jurisdictions

HCD's vendor lacked adequate internal controls over the application review process for Option C jurisdictions. Specifically, the vendor did not have procedures in place to prevent duplicate Option C applications from being processed, to prevent duplication of benefits, or to prevent other errors resulting in improper payments. We identified \$58,055 in improper payments that were approved and disbursed by the vendor. We also identified an additional \$148,168 in pending improper payments that the vendor would have made had we not identified them during our pre-payment audits. The payments were improper because they should have been paid by the Option C jurisdiction rather than by HCD. In addition, two Option C jurisdictions refused to share data with the State, making it impossible to prevent duplication of SRAP benefits within those jurisdictions, which placed HCD at risk of making payments to applicants who had already received assistance from the local jurisdiction.

An Option C jurisdiction is a city or county that elected to self-administer its direct federal allocation of rental assistance funds through its own local program, but elected to have the State administer its proportionate SRAP share. Each Option C jurisdiction was required to develop and execute a partnership agreement with the State to safeguard SRAP funds from duplication of benefit, fraud, and abuse. HCD provided SCO auditors with access to the vendor's database, which includes data about assistance that individuals have already received. To prevent duplication of benefits, CMs are to refer to this database when processing applications for Option C jurisdictions.

City and County of San Francisco

The partnership agreement between the State and the City and County of San Francisco gave the State responsibility for providing rental assistance between April 2020 and March 2021 (the arrears period), and the city and county responsibility for providing rental assistance for April 2021 and after (the prospective period).

In the June 7, 2021 weekly pay file, we identified 29 improper payments to applicants in the City and County of San Francisco, totaling \$58,055. HCD's vendor improperly approved payments for the prospective period (April 2021 through June 2021). We also identified an additional 108 transactions for the same period, totaling \$148,168, in the June 14, 2021 pay file. Because we informed HCD of the error before payment was initiated, the 108 transactions were removed from the pay file. Neither the vendor nor HCD had a process in place to ensure that CMs did not approve prospective period rent payments for applicants in the City and County of San Francisco. We did not include these errors in the amount quantified in Finding 2.

Santa Clara County and City of San Jose

HCD representatives stated that two Option C jurisdictions—Santa Clara County and the city of San Jose—refused to share data with the State. Without access to a jurisdiction’s information about assistance provided to applicants, HCD could not ensure that duplication of benefits did not occur.

Per the partnership agreements with these local jurisdictions, the State would process applications submitted through the state program from the beginning of the program until April 30, 2021. After that date, the State would assist only low-income residents, or households with income greater than 30% of the area median income. The local jurisdictions would assist extremely low-income residents, or households with incomes at or below 30% of the area median income. However, HCD’s vendor improperly processed applications for extremely low-income residents who should have been redirected to the local program. Pursuant to the agreements, the State was to process applications only for low-income residents. Furthermore, because these two jurisdictions refused to share program data, HCD and, consequently, SCO could not determine whether duplication of benefits occurred.

After the review period, all Option C jurisdictions were asked to choose Option A or Option B. There are currently no Option C jurisdictions in California. Therefore, these errors should not recur, unless Option C jurisdictions are reinstated and internal controls are not improved.

Health and Safety Code section 50897.3(b)(2)(B) states:

(i) To minimize legal liability and potential noncompliance with federal law, specifically those violations described in Section 501(k)(3)(B) of Subtitle A of Title V of Division N of the federal Consolidated Appropriations Act, 2021 (Public Law 116-260), the department, or, if applicable, the program implementer, shall request that grantees described in this paragraph enter into a data sharing agreement for the purpose of preventing unlawful duplication of rental assistance to eligible households.

(ii) Notwithstanding any other law, a grantee that enters into a data sharing agreement required by this subparagraph may disclose personally identifying information of rental assistance applicants to the department or the program implementer for the purposes described in this subparagraph.

(iii) A grantee described by clause (ii) shall provide all applicable data, as determined by the department, before the department or program implementer begins administering funds within the grantee’s jurisdiction.

GC sections 13400 through 13407 require state agencies to establish and maintain systems of internal control, as fraud and errors are more likely to occur from a lack of effective systems of internal control when active monitoring measures are not maintained to ensure that controls are functioning properly.

In addition, 2 CFR part 200.303 states:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework,” issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). . . .
- (c) Evaluate and monitor the non-Federal entity’s compliance with statutes, regulations, and the terms and conditions of Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings. . . .

Recommendation

We recommend that HCD:

- Recover improper payments; and
- Establish adequate internal control policies and procedures to ensure that the vendor’s CMs process applications in accordance with partnership agreements if Option C is chosen by local jurisdictions at a future date.

HCD’s Response

HCD disagrees with this finding simply based upon the timing of the program operations as it relates to local jurisdictions. As provided under state law SB 91 (Chapter 2, Statutes of 2021), HCD did not have direct regulatory authority over the operations of Option C jurisdictions, or simply put, cities and/or counties that opted to administer their own local emergency rental assistance programs. The SCO raises concern that HCD’s vendor, HORNE, lacked proper controls over Option C jurisdictions. Operating as independent jurisdictions, the state and its vendors had no authority to provide oversight related to the Option C jurisdictions, whereby their use of federal funds, and corresponding oversight, was managed through the U.S. Treasury. HCD respectfully requests this finding be removed from the report as the state, and by extension, its vendor, had no authority over Option C jurisdictions and their payments.

Additionally, this finding does not consider the timing and implementation of Assembly Bill 832 (2021). With the passage of AB 832, effective June 28, 2021, state law required previous Option C jurisdictions to consolidate their operations as a condition of receiving state block grant funds. The enactment of AB 832, and subsequent statutory changes governing the operation of Option C jurisdictions, directly overlaps and conflicts with the time period of the report review. Further, through the execution of amendment #1 with the ERAP fund disbursement vendor, the project set up an additional control through the “Option C Data Lookup Portal” for Option C jurisdictions to inquire

about cases under local program review against state ERAP for the purpose of de-duplication. The City of San Jose, County of Santa Clara, and City/County of San Francisco were all users of this process.

The establishment of the data portal presented the local programs with the appropriate mechanism to ensure local efforts were not duplicative with the state-administered assistance. SB 91 also provided several statutory requirements to address the potential duplication of efforts of Option C localities running local rental assistance programs concurrent with the state, specifically as it related to the increased risk of duplication of benefits. These controls were operationalized by HCD by requiring Option C localities enter into data sharing agreements and utilize the data portal for the purpose of preventing unlawful duplication of rental assistance to eligible households. SB 91 also included a provision that indemnified the state, HCD, and the program implementer acting on behalf of the department, from liability in the Option C localities' administration of assistance.

SCO Comment

Our finding and recommendation remain unchanged. This finding is not related to the timing of program operations or a lack of controls over Option C jurisdictions. We identified payments approved by HCD's vendor to applicants who reside in Option C jurisdictions, and the approved payments did not follow the partnership agreement between HCD and the Option C jurisdictions. We believe that the vendor's internal controls should be strengthened to help ensure that payments consistently adhere to the partnership agreements.

FINDING 5— Pay files subject to change and unreliable

HCD's vendor submitted weekly pay files to HCD for approval for payment and issuance of funds to be disbursed. However, the vendor added or subtracted payments to be paid after submitting the weekly pay file to HCD for approval. Furthermore, amounts recorded in the weekly pay files did not reconcile to approved disbursement amounts in the Neighborly application. As a result, we could not rely on the provided pay files to determine the actual amount disbursed for each applicant or the number of applicants to be paid. If these deficiencies are not mitigated, payments may be made that differ from what HCD approves.

Unapproved pay file modifications

HCD's vendor submits a weekly pay file to HCD for review and approval. However, subsequent to submitting the pay file, the vendor was able to add and subtract payments to the list of funds to be disbursed. In addition, the vendor was able to modify the amounts to be disbursed to the applicants listed in the pay file. According to HCD and its vendor, pay files should represent applications that have been fully reviewed and cleared for payment by the vendor. However, when we communicated errors or miscalculations related to the applications that we reviewed, oftentimes the vendor stated that either the applications had been withheld for further review, or that approved payment amounts had been modified subsequent to submission of pay files to HCD.

Disbursements not reconciled to approved payments

HCD receives a pay file from its vendor each week for review and approval. HCD then transfers funds to the vendor for the total amount of all transactions contained in the pay file that the vendor submitted for approval. HCD does not reconcile the individual amounts paid (as shown on bank statements) to the tenant case IDs and individual amounts approved for payment in the weekly pay files. Instead, HCD reconciles only the total dollar amounts; specifically, HCD reconciles the total amount transferred to the vendor to the total dollar amount reported on the monthly bank statements.

Duplicate payment identification

HCD's vendor submits a pay file each week for review and approval by HCD. The pay file should represent the number of applications that have been reviewed and approved by the vendor's CMs and QA/QC staff, and should reconcile to data from the Neighborly application. We analyzed the transactions in the weekly pay files submitted for approval during the review period, and identified 326 transactions, totaling \$2,560,378, that were duplicate payments. We identified 163 applicants who, according to the pay files submitted, may have been paid more than once for the same rental periods and/or dollar amounts.

In 144 transactions, 72 applications had different invoice numbers. In the other 182 transactions, 91 applications had duplicate invoice numbers. Representatives for HCD's vendor indicated that the payment system will not process duplicate invoice numbers; however, we found payment transactions for the same specific period of time in several pending pay files. In some cases, these pay files waiting for approval had the same invoice number, and in other cases the invoice numbers were different. We cannot determine whether payments were made multiple times or if approved payments were not made promptly, then were included in a subsequent pay file, approved for payment a second time, and finally paid.

As previously mentioned, HCD and its vendor have the ability to verify that duplicate payments have not been made. However, HCD and its vendor do not reconcile disbursements to payments previously approved in the weekly pay file at the individual transaction level. Therefore, we could not determine whether these transactions were for duplicate payments or were receipt of transactions that appeared in multiple pay files.

Following are examples of pay file variances that we identified.

Example 1

In the June 14, 2021 pay file, we identified a \$1,600 transaction for one applicant that was listed twice, and a \$4,160 transaction for another applicant that was listed twice. We inquired with HCD regarding these transactions. HCD indicated that the vendor had identified these duplicate amounts before payment was processed. However, after reviewing the two applications in Neighborly, we found that one of the erroneous payments had not been corrected. A \$1,600 payment was disbursed twice, resulting

in an overpayment. HCD representatives indicated that HCD would work with its vendor to establish processes and procedures to ensure that coding errors are eliminated prior to pay file generation. As of the date of this report, we have not received from HCD a description of any such procedure or process.

Example 2

Two payments of \$18,560, both for the same applicant, appeared in the June 21, 2021 pay file. In Neighborly, the budgeted items totaled \$29,800. However, the total amount disbursed was \$46,710, representing an overpayment of \$16,910. Instead of keying the correct prospective rent amount of \$1,650 ($\$6,600 \times 25\%$), vendor staff members keyed the rental arrears amount of \$18,560 twice.

Example 3

A payment of \$16,476 for an applicant appeared in the May 3, 2021 and June 1, 2021 pay files. Although we noted that the disbursement information in Neighborly displayed only one of the amounts, the application's audit log indicated that a duplicate payment had been made, and the transaction information in Neighborly had been deleted. Without the actual disbursement information, we cannot verify that no duplicate payments occurred.

GC sections 13400 through 13407 require state agencies to establish and maintain systems of internal control, as fraud and errors are more likely to occur from a lack of effective systems of internal control when active monitoring measures are not maintained to ensure that controls are functioning properly.

In addition, 2 CFR part 200.303 states:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework," issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). . . .
- (c) Evaluate and monitor the non-Federal entity's compliance with statutes, regulations, and the terms and conditions of Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings. . . .

Recommendation

We recommend that HCD implement adequate internal control policies and procedures, such as a reconciliation process, to ensure that all amounts disbursed were included in the approved pay files.

HCD's Response

HCD disagrees with this finding. Since program inception, there was a clear understanding that pay files would shift as various reviews by Bill.com, HCD, HORNE, and SCO identified irregularities. The SCO statement that "HCD's vendor modified and processed pay files without HCD's approval of the adjustments" does not reflect the true nature of the expected changes to pay files that occur on a weekly basis.

The payment file submitted to HCD each Monday, is, and has always been, a tentative file that is meant to be corrected/adjusted based on SCO and HCD review inputs. During the weekly review period (Monday – Thursday), files identified by SCO (when SCO was involved in pre-payment review) and by HCD (by both HCD Internal Control Auditors and program) to be potentially fraudulent or irregular are pulled from the payment file and forwarded to vendor for additional review. Files with discrepancies on approved amounts are logged and shared with vendor so corrective actions can be taken. This process results in a dynamic payment file where files presented on Monday may be modified/removed by Thursday. This process was reviewed and discussed with the SCO as the program established the pre-payment review process in April 2021.

The process established by HCD in coordination with SCO and the vendor was determined to be a best practice for ERAP programs. This information has been shared with other states and local jurisdictions for implementation.

SCO Comment

Our finding and recommendation remain unchanged. During the review period, it was our understanding that the pay file comprised applications that the vendor had reviewed, approved, and submitted to HCD for approval for payment. In April 2021, SCO understood that actual payments might be adjusted based on reviews by HCD and SCO. However, the dynamic nature of the payment file results in a potential risk of duplicate payments as described above, especially as the individual amounts paid were not reconciled to the approved payments.

HCD did not provide comments on the three examples of pay file variances presented in the finding.

FINDING 6— Additional oversight of Option B jurisdictions recommended

In addition to current monitoring procedures, HCD should conduct additional on-site monitoring of Option B jurisdictions based on a risk assessment to ensure compliance with executed standard agreements and federal program guidelines.

Option B jurisdictions receive their proportionate SRAP shares through block grants. To receive this funding, local jurisdictions must execute standard agreements with HCD. Each jurisdiction must submit a work plan in accordance with SRAP guidelines before the standard agreements are executed. Option B jurisdictions receive, approve, and pay tenant and landlord SRAP assistance according to standard agreements. During our initial survey of the program, HCD indicated that it planned to ensure proper oversight and monitoring of Option B jurisdictions by periodically

reviewing approved tenant and landlord applications to ensure that Option B jurisdictions were in compliance with work plans and program requirements. We inquired with HCD regarding this oversight procedure during our review. HCD representatives stated that it did not plan to review applications from individual jurisdictions, and that it was the local jurisdiction's responsibility to follow work plans submitted to HCD.

Without the necessary oversight, HCD cannot provide assurance that Option B jurisdictions are expending their proportionate SRAP shares in accordance with executed standard agreements between the jurisdiction and HCD, and that Option B jurisdictions are complying with federal program requirements.

2 CFR part 200.332, subparagraph (b) requires all pass-through entities to:

Evaluate each subrecipient's risk of noncompliance with Federal statutes, regulations, and the terms and conditions of the subaward for purposes of determining the appropriate subrecipient monitoring described in paragraphs (d) and (e) of this section, which may include consideration of such factors as:

- (1) The subrecipient's prior experience with the same or similar subawards;
- (2) The results of previous audits including whether or not the subrecipient receives a Single Audit in accordance with Subpart F of this part, and the extent to which the same or similar subaward has been audited as a major program;
- (3) Whether the subrecipient has new personnel or new or substantially changed systems; and
- (4) The extent and results of Federal awarding agency monitoring (*e.g.*, if the subrecipient also receives Federal awards directly from a Federal awarding agency).

2 CFR part 200.332, subparagraph (d) further requires all pass-through entities to:

Monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved. Pass-through entity monitoring of the subrecipient must include:

- (1) Reviewing financial and performance reports required by the pass-through entity.
- (2) Following-up and ensuring that the subrecipient takes timely and appropriate action on all deficiencies pertaining to the Federal award provided to the subrecipient from the pass-through entity detected through audits, on-site reviews, and written confirmation from the subrecipient, highlighting the status of actions planned or taken to address Single Audit findings related to the particular subaward.
- (3) Issuing a management decision for applicable audit findings pertaining only to the Federal award provided to the subrecipient from the pass-through entity as required by § 200.521.
- (4) The pass-through entity is responsible for resolving audit findings specifically related to the subaward and not responsible for resolving crosscutting findings. If a subrecipient has a current Single

Audit report posted in the Federal Audit Clearinghouse and has not otherwise been excluded from receipt of Federal funding (*e.g.*, has been debarred or suspended), the pass-through entity may rely on the subrecipient's cognizant audit agency or cognizant oversight agency to perform audit follow-up and make management decisions related to cross-cutting findings in accordance with section § 200.513(a)(3)(vii). Such reliance does not eliminate the responsibility of the pass-through entity to issue subawards that conform to agency and award-specific requirements, to manage risk through ongoing subaward monitoring, and to monitor the status of the findings that are specifically related to the subaward.

Recommendation

We recommend that HCD continue current monitoring procedures and increase on-site monitoring of Option B jurisdictions based on a risk assessment to ensure that funds are being administered in accordance with executed standard agreements and federal program guidelines. Monitoring and oversight controls should include a review process for the Option B jurisdictions' applications.

HCD's Response

HCD disagrees with this finding. HCD conducted pre-emptive reviews of Option B jurisdictions prior to preparing any standard agreements for block grant subawards to help ensure the subrecipients would be able, willing, and prepared to comply with the subaward terms, including federal and state law and guidance.

Specifically, HCD received and reviewed each subrecipient's adoption of an authorizing resolution approved by the local governing body. In addition, HCD reviewed each subrecipient's proposed ERA Program Guidelines for conformity with current federal and state guidance. Prior to HCD issuing the standard agreements for state block grant subawards, each subrecipient was required to document their specific program operating criteria in a manner that conformed to applicable federal and state law. Following the reviews of local program guidelines and HCD's concurrence that they materially conformed with the requirements, the guidelines were incorporated as contractual commitments in the respective standard agreement for each subrecipient.

Only one subrecipient of an ERA1 block grant award (City of Stockton) used the awarded funds during the review period covered by the draft SCO report. HCD monitored this subrecipient's performance and use of funds for allowable purposes on a weekly basis using reports provided by the subrecipient. HCD requested and received weekly data detailing the subrecipient's performance in the following criteria:

- a. Weekly and cumulative obligations of state block grant funds for the payment of costs for eligible households use
- b. Weekly and cumulative expenditures of state block grant funds for the payment of costs for eligible households use
- c. Weekly and cumulative obligations of federal direct award funds for the payment of costs for eligible households use
- d. Weekly and cumulative expenditures of federal direct award funds for the payment of costs for eligible households use

- e. Weekly and cumulative Tenant-initiated applications received
- f. Weekly and cumulative Tenant-initiated applications processed
- g. Weekly and cumulative Tenant-initiated applications approved
- h. Weekly and cumulative Landlord-initiated applications received
- i. Weekly and cumulative Landlord-initiated applications processed
- j. Weekly and cumulative Landlord-initiated applications approved

In our view, the activities HCD undertook conform to the standards described in 2 CFR Part 200.332 – ‘Requirements for pass-through entities.’ The applicable section states:

All pass-through entities must:

- (d) Monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved. Pass-through entity monitoring of the subrecipient must include:
 - (1) Reviewing financial and performance reports required by the pass-through entity.
 - (2) Following-up and ensuring that the subrecipient takes timely and appropriate action on all deficiencies pertaining to the Federal award provided to the subrecipient from the pass-through entity detected through audits, on-site reviews, and written confirmation from the subrecipient, highlighting the status of actions planned or taken to address Single Audit findings related to the particular subaward.

HCD’s pre-review of local program guidelines met the initial monitoring conditions specified in 2 CFR 200.332(d), and HCD’s weekly reviews of program performance metrics were adequate and appropriate levels of monitoring to meet the condition specified in 2 CFR 200.332(d)(1) for the initial months of the subrecipient’s use of the subaward funds. Other aspects of subrecipient monitoring described in 2 CFR 200.332(d)(2) will only be feasible after subrecipients have received results from external reviews, audits, and examinations of their programs beyond the responsibility of HCD as a pass-through entity. HCD agrees it is reasonable that additional monitoring criteria, procedures, and examinations are appropriate to maintain ongoing confirmation that subrecipients are continuing to perform in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved.

Furthermore, HCD has maintained consistent communication and oversight of Option B programs after executing each standard agreement for state subawards. As most Option B jurisdictions prioritized utilizing their direct federal funds before expending state block grants, only now, one year into the program, has a significant amount of ERA 1 block grants been expended. As such, additional monitoring is set to commence and HCD has been undergoing a procurement for a qualified firm to provide detailed monitoring of block grant payments by Option B subaward recipients. Any misuse of funds is subject to recapture or repayment under the terms of the Option B standard agreements and state law.

SCO Comment

HCD indicated that it is now in the process of implementing this recommendation by procuring the services of a vendor to provide detailed monitoring of block grant payments made by Option B subaward recipients, and provided additional information regarding other monitoring processes previously implemented. Therefore, we adjusted this finding to remove language stating that HCD is not in compliance with 2 CFR part 200.329, and instead indicated that in addition to current monitoring procedures, HCD should conduct additional on-site monitoring of Option B jurisdictions based on a risk assessment to ensure compliance with executed standard agreements and federal program guidelines. 2 CFR part 200.332, subparagraph (b) requires HCD, as pass-through entity, to perform risk assessments to tailor its sub-recipient monitoring activities. The results of this risk assessment should drive the extent and magnitude of the monitoring activities performed by a pass-through entity on its sub-recipients. The SRAP is a higher risk program because it required Option B jurisdictions to make a high volume of payments to the public in a relatively short time; the SRAP is also fairly complex and the emergency nature of the program did not provide Option B jurisdiction a significant amount of time to prepare for program implementation.

FINDING 7— Corrective actions not verified

HCD did not ensure that its vendor implemented corrective actions for all errors and issues identified by SCO and HCD. SCO notified HCD of errors and issues in various pay files, but HCD did not ensure that its vendor addressed all of the errors identified. Moreover, HCD did not verify corrective actions for all of the errors the vendor addressed. If errors are not addressed and corrected, HCD is at risk of making improper payments and failing to eliminate internal control weaknesses.

HCD's vendor not responding to all SCO comments

HCD contracted with SCO to conduct post-payment audits of approved applications to ensure compliance with program requirements. During the review period, SCO submitted the testing results for each pay file to HCD for review by HCD and its vendor. The testing results were uploaded onto HCD's SharePoint with a column for the vendor's comments. As of August 3, 2021, the vendor provided comments that demonstrated corrective actions only for pay files dated prior to May 17, 2021. In addition, the vendor did not comment on all issues noted by SCO in those pay files, which indicates that these items had not been addressed.

HCD not ensuring vendor corrective actions

HCD did not respond to all issues identified, such as those resulting in monetary errors. Although HCD confirmed that some errors had been corrected, it noted other errors that had not been corrected. In addition, HCD provided no assurance that corrections would be made. Furthermore, some HCD comments indicated that the vendor's calculations were incorrect, but no action was taken to correct the miscalculations.

As of July 9, 2021, HCD had not provided documentation in response to our inquiries that support its performance of oversight activities to ensure that its vendor responded to all issues noted by SCO. On July 15, 2021, HCD indicated that it was maintaining a log of all issues reported by SCO and HCD, which it would review to ensure that the vendor implemented corrective actions.

HCD also reviewed applications to test its vendor's processing of applications. HCD representatives stated that its vendor will track and adjust future payments to correct any errors that HCD identifies. However, HCD representatives did not indicate that HCD would ensure that the vendor implements these corrections.

GC sections 13400 through 13407 require state agencies to establish and maintain a system of internal control, as fraud and errors are more likely to occur from a lack of effective systems of internal control when active monitoring measures are not maintained to ensure that controls are functioning properly.

In addition, 2 CFR part 200.303 states:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in "Standards for Internal Control in the Federal Government" issued by the Comptroller General of the United States or the "Internal Control Integrated Framework," issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). . . .
- (c) Evaluate and monitor the non-Federal entity's compliance with statutes, regulations, and the terms and conditions of Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings. . . .

Recommendation

We recommend that HCD:

- Require its vendor to implement corrective actions to address all errors identified by SCO and HCD in a timely manner;
- Conduct monitoring procedures to verify that the vendor implements corrective actions in a timely manner for all errors identified by HCD and SCO; and
- Verify that the vendor adequately adjusts payments in response to application errors identified.

HCD's Response

HCD disagrees with this finding. As of the date of the draft SCO report, HCD has followed up on and resolved all the payment discrepancies identified by the SCO. However, due to the timing of this review, the resolved findings were not reviewed by SCO.

SCO Comment

Our finding and recommendation remain unchanged. As stated in this report, the finding referred to the period from the beginning of the program through June 30, 2021. During the review period, HCD did not ensure that corrective actions were implemented for all issues that we identified and communicated. Additionally, the finding states that on July 15, 2021, HCD indicated that it was maintaining a log of all issues reported by SCO and HCD, which it would review to ensure that the vendor implemented corrective actions. We appreciate that HCD indicated in its response that it has followed up on and resolved all of the payment discrepancies identified by SCO.

FINDING 8— Inadequate control procedures and documentation requirements to mitigate risk of fraud

HCD did not establish adequate control procedures regarding landlord and tenant documentation requirements necessary to mitigate the risk of fraud and misuse of funds. Specifically, HCD did not require documentation to substantiate landlords' property ownership and to ensure that tenants were eligible for the rental assistance amounts requested. HCD did not establish policies and procedures for the vendor to limit tenant assistance to three months of rent owed when tenants were unable to provide landlord contact information or adequate proof of outstanding rental obligations. Furthermore, HCD did not establish policies and procedures to ensure that its vendor retains tenant records and effectively evaluates whether tenants are eligible to receive rental assistance in excess of three months.

Landlord applications

At the initiation of the program, landlords were required to substantiate property ownership with one of the following documents: recorded property deed, property tax form, or proof of homeowner's insurance. Documents that originate from a third party may be more reliable and can be verified with the third party. However, as of April 28, 2021, HCD no longer requires landlords to provide such verification of ownership. Instead, HCD requires only a completed Form W-9 (Request for Taxpayer Identification Number and Certification), lease agreement, and rent ledger, none of which are produced by a third party.

The change in required documentation was intended to reduce application processing times. However, HCD's reliance on self-reported information increases the risk of fraud and misuse of funds. The Form W-9, lease agreements, and rent ledgers are all completed or created by the individuals applying for SRAP funds. If HCD does not require supporting documentation from government or other third-party sources to verify ownership, the SRAP is vulnerable to a higher risk of fraud.

Tenant applications

HCD lacked documentation requirements and outreach effort procedures to ensure that tenants were eligible for the rental assistance amounts requested. Additionally, payments were issued directly to tenants without third-party verification. Furthermore, the vendor's Landlord Outreach Team did not obtain contact information from landlords; instead, it relied on phone numbers and email addresses provided by tenant applicants. If a landlord did not respond to a tenant's rental assistance application within the allowed timeframe, then payment was issued to the tenant. Without verification of landlord contact information, tenant applicants may receive improper payments by providing falsified landlord contact information.

In addition, until December 2021, when HCD changed program requirements, the application requirements did not demand adequate proof of rental obligations from tenants. The application requires a tenant to provide only a lease agreement or month-to-month rental agreement as evidence of rent owed. Although these documents may establish where the applicant resides and the rental payment amount, they do not provide evidence of the amount of rental obligation. Therefore, SRAP funds could have been paid directly to a tenant without proof of rental obligation or any contact with a landlord.

In order to provide relief to tenants whose landlords have been unresponsive or unavailable the U.S. Treasury's guidelines for the Emergency Rental Assistance Program permit the grantee (HCD) to issue up to three months of rental assistance with only a written attestation of rental obligation. However, after providing assistance for three months, grantees must obtain evidence of rent owed before providing further assistance to applicants. During the review period, HCD did not establish policies and procedures that require its vendor to keep records of which applicants received assistance based on written attestations to ensure that these applicants do not receive further assistance until they provide proof of rent owed.

The response to question number 5 of the U.S. Treasury's "Emergency Rental Assistance Program" FAQ states, in part:

If an applicant is able to provide satisfactory evidence of residence but is unable to present adequate documentation of the amount of the rental obligation, grantees may accept a written attestation from the applicant to support the payment of assistance up to a monthly maximum of 100% of the greater of the Fair Market Rent or the Small Area Fair Market Rent for the area in which the applicant resides. . . .The assistance described in this paragraph may only be provided for three months at a time, and a grantee must obtain evidence of rent owed consistent with the above after three months in order to provide further assistance to such a household; Treasury expects that in most cases the household would be able to provide documentation of the amount of the rental obligation in any applications for further assistance.

2 CFR part 200.303 states:

The non-Federal entity must:

- (a) Establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and the terms and conditions of the Federal award. These internal controls should be in compliance with guidance in “Standards for Internal Control in the Federal Government” issued by the Comptroller General of the United States or the “Internal Control Integrated Framework,” issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). . . .
- (c) Evaluate and monitor the non-Federal entity’s compliance with statutes, regulations, and the terms and conditions of Federal awards.
- (d) Take prompt action when instances of noncompliance are identified including noncompliance identified in audit findings. . . .

Recommendation

We recommend that HCD:

- Reinstate the requirement for landlord applications to include verifiable third-party documentation that substantiates property ownership;
- On tenant applications, require landlords to confirm their choice to opt out of the program when applicable;
- Require verification from landlords of their tenants’ rental obligations, consistent with U.S. Treasury guidelines;
- Monitor HCD’s vendor to ensure that, if a tenant provides only an attestation form and does not provide the supporting documentation required by the program, tenant payments are limited to three months of rent owed; and
- Recover overpayments beyond three months of rent to applicants who provided only attestation forms and did not provide the supporting documentation required by the program.

HCD’s Response

HCD partially agrees with this finding and will continue to implement recommendations wherever possible. As previously noted, improvements have been made since the scope period of the SCO review, and the presentation of the draft review. HCD would like to provide clarification regarding some findings in this review as follows:

- Reinstate the requirement for landlord applications to include verifiable third-party documentation that substantiates property ownership.

HCD Process Implemented

Landlord proof of ownership was implemented as a process change in December 2021 followed by the vendor's incorporation of third-party verification tool in February 2022. At this point, the state program had deployed X40% of total resources to expended to date.

- On tenant applications, require landlords to confirm their choice to opt out of the program when applicable.

HCD Process Implemented

As part of the case management process, the vendor implemented changes that require the case managers attempt to verify landlord participation by making at least three (3) attempts to contact the listed landlord over a 5-business day period. Failure of the landlord to provide an application and required documentation in that time frame will result in the landlord opting out.

- Require verification from landlords of their tenants' rental obligations, consistent with U.S. Treasury guidelines.

HCD Response

For participating landlords, case management team does request a copy of current ledger to verify tenant's rental obligations. HCD considers the process of verification of the tenant's request by the landlord, consistent with U.S. Treasury guidelines.

- Monitor HCD's vendor to ensure that, if a tenant provides only an attestation form and does not provide the supporting documentation required by the program, tenant payments are limited to three months of rent owed.

HCD Response

This recommendation is not in alignment with the mandate set forth in AB 832 to compensate 100% of the eligible household's unpaid rental debt accumulated on or after April 1, 2020. There is not a limitation of 3 months of rent owed.

In addition, it is not in alignment with the U.S. Treasury guidelines as it pertains to attestations.

- Recover overpayments beyond three months of rent to applicants who provided only attestation forms and did not provide the supporting documentation required by the program.

HCD Response

SCO's statement "The HCD did not establish adequate control procedures regarding landlord and tenant documentation requirements necessary to mitigate the risk of fraud and misuse of funds" is inconsistent with U.S. Treasury guidance that clearly allows for HCD to rely on attestations, which the program initially did. Concurrently, program staff created a risk profile and subsequently utilized the risk profile to adjust requirements. The program does require additional documentation based on adjustments that were implemented; this finding does not take into account the continuous improvements and misstates actions done in conjunction with the SCO.

In addition to the above, HCD internally pulls target samples and reviews 80-100 applications from the pre-payment file for additional review specifically looking for cases and patterns of fraudulent activity that cannot be easily identified through the vendors process and procedures. HCD internally tracks all files escalated to the vendor for additional review and follows up on the results of those reviews and outcomes.

SCO Comment

Our finding and recommendation remain unchanged. Our finding reflects the internal controls and program requirements as of June, 30, 2021. SCO recognizes that HCD has since implemented internal controls and adjusted program requirements to strengthen program controls.

As stated in the finding, the U.S. Treasury's FAQ indicates that payment of assistance for written attestations of rent owed may be provided only for three months at a time until further evidence is obtained for additional assistance. If the tenant is not able to provide additional supporting documentation, only then should the payment be limited to three months of rent owed. During our review of payments, we identified instances in which payments were made beyond the three-month limit, although the application file contained no documentation other than the self-attestation form to substantiate the amount of rent owed. It should be noted that this rule does not conflict with AB 832 because it does not prevent tenants from receiving 100% of eligible rent owed once proper documentation has been received.

**Attachment—
California Department of Housing and Community
Development’s Response to Draft Review Report**

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July 15, 2022

Kimberley Tarvin, CPA
Chief, Division of Audits
California State Controller

Dear Ms. Tarvin,

The California Department of Housing and Community Development (HCD) would like to thank the State Controller's Office (SCO) for the final review report on HCD's oversight of the State Rental Assistance Program (SRAP). Entering a partnership with the SCO at the onset of this program resulted in proactive actions to protect renters, landlords, and public funds.

Given the unprecedented nature of the program, it was critical that we worked together to proactively identify opportunities for improvement, ensuring program improvements could be made while the program was being administered, instead of an approach that was focused on changes after the fact. This constructive approach and partnership provided the ability for HCD to implement changes recommended by SCO and adapt to the everchanging circumstances faced by a program of this size and scale. Of note, based on the SCO initial draft report for the same time period included in this final report, HCD and its third-party vendor HORNE addressed the initial observations to ensure the program continued to make refinements on the backend while not slowing the pace of disbursement of funds. Our commitment has always been to keep Californians housed, make landlords whole, and act as good stewards of public funds.

Well in advance of the initial draft report provided in March 2022, HCD and its vendors worked diligently to respond to ongoing feedback from SCO, resulting in the following achievements:

- The program has worked diligently to minimize fraud attempts while keeping barriers to program participation low. Compared to other public assistance and rent relief programs, our efforts resulted in significantly lower rates of fraud while far outpacing other emergency rental assistance programs across the country.
- After early conversations with the SCO, HCD and HORNE implemented a full reconciliation process between Bill.com and the program's weekly pay files. This policy ensured that every payment would be properly accounted for and traceable to a tenant or landlord in each payment file. This reconciliation process has been identified as a national best practice and has been adopted by other emergency rental assistance programs.

HCD takes this final report seriously and we are committed to adequately and expeditiously addressing any new concerns to the extent feasible. As California's rent relief program is winding down and very few applications remain in the queue, some recommendations may no longer be relevant or applicable. HCD will note these recommendations in best practices reporting as we are always seeking ways to improve how we support California's underserved communities.

Please see below for a detailed response to the SCO's review. As noted, because of our partnership with SCO since the inception of the program, some of these findings have already been addressed and program operations quickly adopted process improvements following the draft report. In an effort to provide a thoughtful and transparent response while also balancing the integrity of the program and future public programs, some specific fraud-prevention measures have not been explained in detail. We feel our response adequately addresses program changes without making public information that could aid individuals seeking to exploit other programs.

Finding 1 - Potential fraud identified

HCD Management Response

HCD partially agrees with this finding for the initial cases identified; however, as noted above, HCD implemented many process improvements since the initial SCO review was conducted. HCD will continue to identify, where applicable, recommendations that can be taken into consideration with the limited time left in the program as well as in future emergency housing initiatives.

Specific findings of the review are addressed below:

Duplicate landlord and case IDs

The Program is focused on preventing multiple/duplicate tenant applications per property (address and unit) that could result in duplicate benefits being paid. Within this focus and the daily operation, it is common for a large landlord to have multiple applications because larger landlords may have multiple properties and multiple management companies. Benefits are approved and awarded based on a qualified tenant, not a qualified landlord.

The program does track instances of multiple landlord applications as the review notes, but this condition alone is not an issue since awards are based solely on tenant eligibility. Only combined with other factors do instances of multiple landlord applications then begin to indicate potential fraud.

Potentially fraudulent supporting documentation

For the period between 7/1/2021 thru 12/31/2021, ERAP approved 201,000 tenant applications. The identified 488 "potentially" fraudulent applications translate to 0.2% of all approved ERAP applications processed during this period. With over \$1.5 billion disbursed, the \$7 million in funds disbursed to potentially fraudulent applications represents 0.4% of all funds disbursed during the same period. The Program has worked closely with SCO and other state and federal partners to minimize the incidence as well as undertaking efforts to recapture any funding that has been disbursed.

Documentation requirements and staff training have continued to evolve throughout the duration of the program. As strongly recommended through program guidance provided by the U.S. Treasury, the program provides various alternative documentation options for applicants to submit, depending on their circumstances. Documentation submitted, will therefore vary. HCD and its vendor have continuously sought to ensure staff are equipped to identify potentially fraudulent documentation. This is, in part, the reason HCD contracted with the SCO to help provide additional third-party verification. The strong partnerships between SCO and HCD, as well as HCD and the third-party vendor, allowed program staff to continue focusing on disbursing funds while broader programmatic improvements were initiated.

Recommendations

In regard to the multiple recommendations, we have a few comments, while acknowledging we do not disagree and will proactively implement them where appropriate. Our comments are as follows:

- As previously noted, HCD has seen instances where large landlords (or property management companies with multiple agents) manage multiple properties, therefore creating multiple landlord files. As stated in the previous response, multiple landlord case files are not unusual. The Program focus is on duplicate tenant case files and preventing multiple tenant applications for the same property.
- The vendor provides fraud training to all case managers in their employee orientation. There are also stand-down presentations for fraud as well as recorded fraud trainings. Additionally, the vendor has a dedicated and seasoned team of resources in place to undertake fraud review. HCD can provide a sample of the specific onboarding fraud training, presentations as well as the recorded training module. It is also important to note that the vendor has extensive experience in delivering large programs and projects nationally and is accustomed to working with federal funds. The vendor's core service is accounting and has served as the prime contractor for disaster recovery and direct service programs.

In response to earlier SCO recommendations, HCD implemented internal control reviews, whereby HCD Internal Control Auditors, select and review approved applications prior to payment disbursement. Performed weekly, applications are reviewed for documentation completeness, eligibility, assistance amount approved, and checked for landlord property ownership where applicable. HCD Internal Control Auditors also conducted data analysis on specific application and assistance attribute to locate potentially fraudulent cases for additional review.

- In September 2021, the vendor implemented a policy to address high dollar rents. This policy limits the monthly rent assistance available on any given property to not exceed a certain percentage above HUD's Fair Market Rent (FMR).
- In December 2021, the vendor instituted the requirement that participating landlords must provide third-party documentation supporting proof of property ownership. In

February 2022 the vendor incorporated a business subscription with the ability to verify public records, thereby providing the vendor and their fraud unit the ability to research various public records.

- HCD has reviewed the potential fraudulent applications identified by SCO, and those suspected applications have been denied and a recapture has been initiated. HCD is developing a procedure working with the California State Franchise Tax Board to intercept funds not recaptured/repaid by a fraudulent applicant as well as partnering with law enforcement.

Finding 2 - Verification procedures not consistently or effectively performed resulting in overpayments and underpayments

HCD Management Response

It is important to note that HCD was in the process, and has since finalized, the recommended improvements provided at the time of SCO's review.

However, portions of the findings stated in the SCO review require clarification:

- The basis for this finding stems from the requirement provided in Senate Bill (SB) 91, effective January 29, 2021, originally limiting the program to provide partial compensation for both direct to landlord and direct to tenant payments. This statutory requirement was subsequently amended following the passage of Assembly Bill (AB) 832, effective June 28, 2021, authorizing the program to provide compensation for 100-percent of rent owed to be paid. Following the enactment of AB 832, the vendor was able to go back and pay the remaining balance of unpaid rent (top-off) attributed to the previous partial compensation requirements the program was required to follow under state law. Any overpayments from the early months were taken into consideration in the top-off payment by discounting the top-off disbursement. HCD can provide the total count of applications and amounts paid through this process.
- This is a datapoint specific to the first three months of the program. As such, the total number of cases reviewed represents less than 3% of volume to date.

Finding 3 - Death match verification not consistently requested before payment approved

HCD Management Response

HCD disagrees with this finding, as the SCO review did not identify any payment disbursed to an application submitted by a deceased person. Since program inception, the program has had a death match verification process and internal controls in place. This process is utilized in the review of all files before payment is issued. The vendor performs procedures developed by HCD in collaboration

with SCO, including requiring the case manager to verify applicant identification against death roll records obtained by a third-party vendor.

Finding 4 - Inadequate controls over Option C jurisdictions

HCD Management Response

HCD disagrees with this finding simply based upon the timing of the program operations as it relates to local jurisdictions. As provided under state law SB 91 (Chapter 2, Statutes of 2021), HCD did not have direct regulatory authority over the operations of Option C jurisdictions, or simply put, cities and/or counties that opted to administer their own local emergency rental assistance programs. The SCO raises concern that HCD's vendor, HORNE, lacked proper controls over Option C jurisdictions. Operating as independent jurisdictions, the state and its vendors had no authority to provide oversight related to the Option C jurisdictions, whereby their use of federal funds, and corresponding oversight, was managed through the U.S. Treasury. HCD respectfully requests this finding be removed from the report as the state, and by extension, its vendor, had no authority over Option C jurisdictions and their payments.

Additionally, this finding does not consider the timing and implementation of Assembly Bill 832 (2021). With the passage of AB 832, effective June 28, 2021, state law required previous Option C jurisdictions to consolidate their operations as a condition of receiving state block grant funds. The enactment of AB 832, and subsequent statutory changes governing the operation of Option C jurisdictions, directly overlaps and conflicts with the time period of the report review. Further, through the execution of amendment #1 with the ERAP fund disbursement vendor, the project set up an additional control through the "Option C Data Lookup Portal" for Option C jurisdictions to inquire about cases under local program review against state ERAP for the purpose of de-duplication. The City of San Jose, County of Santa Clara, and City/County of San Francisco were all users of this process.

The establishment of the data portal presented the local programs with the appropriate mechanism to ensure local efforts were not duplicative with the state-administered assistance. SB 91 also provided several statutory requirements to address the potential duplication of efforts of Option C localities running local rental assistance programs concurrent with the state, specifically as it related to the increased risk of duplication of benefits. These controls were operationalized by HCD by requiring Option C localities enter into data sharing agreements and utilize the data portal for the purpose of preventing unlawful duplication of rental assistance to eligible households. SB 91 also included a provision that indemnified the state, HCD, and the program implementer acting on behalf of the department, from liability in the Option C localities' administration of assistance.

Finding 5 - Pay files subject to change and unreliable

HCD Management Response

HCD disagrees with this finding. Since program inception, there was a clear understanding that pay files would shift as various reviews by Bill.com, HCD, HORNE, and SCO identified irregularities. The SCO statement that "HCD's vendor modified and processed pay files without HCD's approval of the

adjustments” does not reflect the true nature of the expected changes to pay files that occur on a weekly basis.

The payment file submitted to HCD each Monday, is, and has always been, a tentative file that is meant to be corrected/adjusted based on SCO and HCD review inputs. During the weekly review period (Monday - Thursday), files identified by SCO (when SCO was involved in pre-payment review) and by HCD (by both HCD Internal Control Auditors and program) to be potentially fraudulent or irregular are pulled from the payment file and forwarded to vendor for additional review. Files with discrepancies on approved amounts are logged and shared with vendor so corrective actions can be taken. This process results in a dynamic payment file where files presented on Monday may be modified/removed by Thursday. This process was reviewed and discussed with the SCO as the program established the pre-payment review process in April 2021.

The process established by HCD in coordination with SCO and the vendor was determined to be a best practice for ERAP programs. This information has been shared with other states and local jurisdictions for implementation.

Finding 6 - Inadequate oversight of Option B jurisdictions

HCD Management Response

HCD disagrees with this finding. HCD conducted pre-emptive reviews of Option B jurisdictions prior to preparing any standard agreements for block grant subawards to help ensure the subrecipients would be able, willing, and prepared to comply with the subaward terms, including federal and state law and guidance.

Specifically, HCD received and reviewed each subrecipient’s adoption of an authorizing resolution approved by the local governing body. In addition, HCD reviewed each subrecipient’s proposed ERA Program Guidelines for conformity with current federal and state guidance. Prior to HCD issuing the standard agreements for state block grant subawards, each subrecipient was required to document their specific program operating criteria in a manner that conformed to applicable federal and state law. Following the reviews of local program guidelines and HCD’s concurrence that they materially conformed with the requirements, the guidelines were incorporated as contractual commitments in the respective standard agreement for each subrecipient.

Only one subrecipient of an ERA1 block grant award (City of Stockton) used the awarded funds during the review period covered by the draft SCO report. HCD monitored this subrecipient’s performance and use of funds for allowable purposes on a weekly basis using reports provided by the subrecipient. HCD requested and received weekly data detailing the subrecipient’s performance in the following criteria:

- a. Weekly and cumulative obligations of state block grant funds for the payment of costs for eligible households use
- b. Weekly and cumulative expenditures of state block grant funds for the payment of costs for eligible households use
- c. Weekly and cumulative obligations of federal direct award funds for the payment of costs for eligible households use

- d. Weekly and cumulative expenditures of federal direct award funds for the payment of costs for eligible households use
- e. Weekly and cumulative Tenant-initiated applications received
- f. Weekly and cumulative Tenant-initiated applications processed
- g. Weekly and cumulative Tenant-initiated applications approved
- h. Weekly and cumulative Landlord-initiated applications received
- i. Weekly and cumulative Landlord-initiated applications processed
- j. Weekly and cumulative Landlord-initiated applications approved

In our view, the activities HCD undertook conform to the standards described in 2 CFR Part 200.332 – ‘Requirements for pass-through entities.’ The applicable section states:

All pass-through entities must:

(d) Monitor the activities of the subrecipient as necessary to ensure that the subaward is used for authorized purposes, in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved. Pass-through entity monitoring of the subrecipient must include:

- (1) Reviewing financial and performance reports required by the pass-through entity.
- (2) Following-up and ensuring that the subrecipient takes timely and appropriate action on all deficiencies pertaining to the Federal award provided to the subrecipient from the pass-through entity detected through audits, on-site reviews, and written confirmation from the subrecipient, highlighting the status of actions planned or taken to address Single Audit findings related to the particular subaward.

HCD’s pre-review of local program guidelines met the initial monitoring conditions specified in 2 CFR 200.332(d), and HCD’s weekly reviews of program performance metrics were adequate and appropriate levels of monitoring to meet the condition specified in 2 CFR 200.332(d)(1) for the initial months of the subrecipient’s use of the subaward funds. Other aspects of subrecipient monitoring described in 2 CFR 200.332(d)(2) will only be feasible after subrecipients have received results from external reviews, audits, and examinations of their programs beyond the responsibility of HCD as a pass-through entity. HCD agrees it is reasonable that additional monitoring criteria, procedures, and examinations are appropriate to maintain ongoing confirmation that subrecipients are continuing to perform in compliance with Federal statutes, regulations, and the terms and conditions of the subaward; and that subaward performance goals are achieved.

Furthermore, HCD has maintained consistent communication and oversight of Option B programs after executing each standard agreement for state subawards. As most Option B jurisdictions prioritized utilizing their direct federal funds before expending state block grants, only now, one year into the program, has a significant amount of ERA 1 block grants been expended. As such, additional monitoring is set to commence and HCD has been undergoing a procurement for a qualified firm to provide detailed monitoring of block grant payments by Option B subaward recipients. Any misuse of funds is subject to recapture or repayment under the terms of the Option B standard agreements and state law.

Finding 7 - Corrective actions not verified

HCD Management Response

HCD disagrees with this finding. As of the date of the draft SCO report, HCD has followed up on and resolved all the payment discrepancies identified by the SCO. However, due to the timing of this review, the resolved findings were not reviewed by SCO.

Finding 8 - Inadequate control procedures and documentation requirements to mitigate risk of fraud

HCD Management Response

HCD partially agrees with this finding and will continue to implement recommendations wherever possible. As previously noted, improvements have been made since the scope period of the SCO review, and the presentation of the draft review. HCD would like to provide clarification regarding some findings in this review as follows:

- Reinstated the requirement for landlord applications to include verifiable third-party documentation that substantiates property ownership.

HCD Process Implemented

Landlord proof of ownership was implemented as a process change in December 2021 followed by the vendor's incorporation of third-party verification tool in February 2022. At this point, the state program had deployed X40% of total resources to expended to date.

- On tenant applications, require landlords to confirm their choice to opt out of the program when applicable.

HCD Process Implemented

As part of the case management process, the vendor implemented changes that require the case managers attempt to verify landlord participation by making at least three (3) attempts to contact the listed landlord over a 5-business day period. Failure of the landlord to provide an application and required documentation in that time frame will result in the landlord opting out.

- Require verification from landlords of their tenants' rental obligations, consistent with U.S. Treasury guidelines.

HCD Response

For participating landlords, case management team does request a copy of current ledger to verify tenant's rental obligations. HCD considers the process of verification of the tenant's request by the landlord, consistent with U.S. Treasury guidelines.

- Monitor HCD's vendor to ensure that, if a tenant provides only an attestation form and does not provide the supporting documentation required by the program, tenant payments are limited to three months of rent owed.

HCD Response

This recommendation is not in alignment with the mandate set forth in AB 832 to compensate 100% of the eligible household's unpaid rental debt accumulated on or after April 1, 2020. There is not a limitation of 3 months of rent owed. In addition, it is not in alignment with the U.S. Treasury guidelines as it pertains to attestations.

- Recover overpayments beyond three months of rent to applicants who provided only attestation forms and did not provide the supporting documentation required by the program.

HCD Response

SCO's statement "The HCD did not establish adequate control procedures regarding landlord and tenant documentation requirements necessary to mitigate the risk of fraud and misuse of funds" is inconsistent with U.S. Treasury guidance that clearly allows for HCD to rely on attestations, which the program initially did. Concurrently, program staff created a risk profile and subsequently utilized the risk profile to adjust requirements. The program does require additional documentation based on adjustments that were implemented; this finding does not take into account the continuous improvements and misstates actions done in conjunction with the SCO.

In addition to the above, HCD internally pulls target samples and reviews 80-100 applications from the pre-payment file for additional review specifically looking for cases and patterns of fraudulent activity that cannot be easily identified through the vendors process and procedures. HCD internally tracks all files escalated to the vendor for additional review and follows up on the results of those reviews and outcomes.

In closing, HCD would like to note that we have moved expeditiously, but with the appropriate due diligence and oversight to implement the ERAP program. To date, the program has helped over 340,000 households and disbursed nearly \$4 billion in rent and utility assistance to the most vulnerable and underserved households throughout the State of California.

Standing up a first of its kind emergency rent relief program in California required significant partnership between HCD, local jurisdictions, third-party vendors, and other state partners such as the SCO. We agree there are areas for improvement and are proud of the quick action taken before, during, and after the draft review was conducted. Keeping Californians housed, making tenants whole, and serving as good stewards of public dollars has remained at the forefront of our efforts since the program was established. We hope that the results of the SCO report as well as the actions taken by HCD staff and vendors will provide helpful use cases and best practices for future programs.

Thank you for this opportunity to respond. Should you have any questions, please contact HCD's Chief Internal Auditor, Michael Mock, Michael.Mock@hcd.ca.gov

Sincerely,



Gustavo Velasquez
Director
California Department of Housing and Community Development

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