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TO: Charles S. Coulter, Deputy Assistant Secretary for Single Family Housing, HU

FROM: Tanya E. Schulze, Regional Inspector General for Audit, Los Angeles Region, 9DGA

SUBJECT: HUD Did Not Always Enforce REO M&M III Program Requirements

Enclosed is the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General (OIG), final results of our review of HUD's Office of Single Family Housing's oversight of its real estate-owned Management and Marketing III program.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, Title 5 United States Code, section 8L, requires that OIG post its publicly available reports on the OIG Web site. Accordingly, this report will be posted at http://www.hudoig.gov. Please note that the OIG determined that some contents of this audit report would not be appropriate for public disclosure and those items have been redacted from this report.

If you have any questions or comments about this report, please do not hesitate to call me at 213-534-2471.

September 18, 2012

HUD Did Not Always Enforce REO M&M III Program Requirements

Highlights

Audit Report 2012-LA-0003

What We Audited and Why

We audited the U.S. Department of Housing and Urban Development's (HUD) oversight of its real estate-owned (REO) Management and Marketing (M&M) III program in response to a HUD, Office of Inspector General (OIG) auditability survey on REO contract administration and as part of OIG's fiscal year 2012 annual audit plan.

What We Recommend

We recommend that the Deputy Assistant Secretary for Single Family Housing (1) develop and implement policies and procedures for oversight of the M&M III program, procedures to ensure that field service managers are paid only for routine inspections that are conducted, and procedures for the P260 system to ensure that bids meeting applicable thresholds based on the listed and appraised values are accepted; (2) review the P260 system and its related controls; (3) finalize and implement the field service manager scorecard; (4) reimburse or request repayment for the field service managers that were underpaid or overpaid; and (5) ensure that HUD receives repayment for routine inspections that were not conducted by field service managers.

What We Found

HUD did not have adequate procedures in place to ensure consistent and adequate enforcement of asset and field service manager contracts. Specifically, (1) list prices were not always reduced according to the marketing plans, (2) bids were approved that did not meet HUD's flexible threshold, (3) bids were rejected that met the marketing plan thresholds, (4) bids that met applicable thresholds were not always counter offered or forwarded to the government technical representative for approval, and (5) properties were not assigned to field service managers based on performance even when HUD identified performance issues. In addition, HUD did not always pay field service managers in accordance with their contracts, resulting in an estimated net underpayment of $553,784 to field service managers.

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BACKGROUND AND OBJECTIVE

The Federal Housing Administration (FHA) administers the single-family mortgage insurance program and insures approved lenders against the risk of loss on properties obtained with FHA-insured financing. In the event of a default on an FHA-insured loan, the lender acquires title to the property by foreclosure, a deed-in-lieu of foreclosure, or other acquisition method; files a claim for insurance benefits and conveys the property to the U.S. Department of Housing and Urban Development (HUD). As a result of acquisitions through the mortgage insurance program and other programs, HUD needs to sell a sizable inventory of single-family homes, making HUD the largest single seller of real estate in the United States.

Since 1999, HUD has outsourced the disposition of its real estate-owned (REO) inventory to private-sector contractors under its Management and Marketing (M&M) program. In June of 2010, HUD awarded contracts under the third generation of M&M. Under previous generations of M&M contracts, M&M contractors were responsible for both maintenance and marketing of HUD's REO properties. Under the M&M III program, these functions became separated. The field service managers are responsible for property maintenance and preservation, and the asset managers are responsible for the sale of the homes. Contracts were also awarded to an oversight monitor and mortgagee compliance manager for the M&M III program; however, we did not review these functions. The oversight monitor, whose contract was terminated, was responsible for informing HUD of the performance of its REO portfolio and the mortgagee compliance manager performs pre- and post-property conveyance services.

With the M&M III program, HUD introduced and implemented the P260 system, which is an Internet based system that serves as the primary system of record for all REO case management transactions. Asset and field service managers are required to scan and upload documents relating to properties, such as inspection reports and photographs, so that HUD can track the disposition activity from conveyance to sale. HUD administers the REO disposition program through the four Homeownership Centers (Centers) located in Atlanta, GA, Denver, CO, Philadelphia, PA, and Santa Ana, CA. Each Center is responsible for a designated geographic area, with the four geographic areas divided into ten contract areas to award contracts to asset and field service managers. There were 23 contracts awarded to asset managers and 31 contracts awarded to field service mangers[1].

In the first two years of the M&M III program, HUD acquired 198,318 properties and sold 201,585. For the properties that were acquired and sold between June 1, 2010 and May 31, 2012, the average bid amount to the appraised as is value was 86 percent.[2]

[1] Asset and field service managers that were awarded contracts in multiple contract areas were separate contracts.
[2] According to the Single Family Data Warehouse. In reviewing the data to determine the average net return, we noted that the reported appraised as is value was based on the most recent appraisal. Therefore, in cases where an updated appraisal was received and the property value either increased or decreased, the average net return was not accurately reflected based on the original value.

Center	Properties acquired[3]	Properties sold
June 1, 2010, to May 31, 2011		
Atlanta	34,271	26,545
Denver	29,876	25,744
Philadelphia	22,379	22,939
Santa Ana	14,710	12,472
Year 1totals	**101,236**	**87,700**
June 1, 2011, to May 31, 2012		
Atlanta	33,009	41,489
Denver	28,582	33,061
Philadelphia	22,387	22,931
Santa Ana	13,104	16,404
Year 2 totals	**97,082**	**113,885**
Combined totals	**198,318**	**201,585**

Our audit objective was to determine whether HUD's policies and procedures provided for efficient and effective oversight of asset managers and field service managers under its M&M III program.

[3] HUD provided data for the first year, including the number of properties that were acquired in the M&M II program and were transitioned to the M&M III program.

RESULTS OF AUDIT

Finding: HUD Did Not Always Enforce REO M&M III Program Requirements

HUD did not always enforce REO M&M III program requirements for asset managers and field service managers. Also, HUD did not ensure that field service managers were always paid in accordance with their contracts. These conditions occurred because HUD did not develop national standard quality assurance procedures or a quarterly performance report but instead allowed varied procedures across the four Homeownership Centers. As a result, HUD's REO properties may not have always been competitively valued, holding time may not have always been minimized, sales may not have always achieved the highest net return, and properties may have been assigned to field service managers that did not perform at a satisfactory level. In addition, we estimated that HUD overpaid 6 field service managers $491,946 and underpaid 15 field service managers $985,582 from June 2011 to January 2012 and 1 field service manager was underpaid $60,148 from January to February 2012.

Asset Manager Contracts Were Not Always Enforced

Given HUD's lack of standard national procedures, the individual procedures developed by the four Centers were not adequate to ensure that the asset manager contracts were always enforced[4]. Specifically, we found

- List prices were not always reduced in accordance with marketing plans,
- Bids were approved that were below HUD's flexible threshold,
- Bids were improperly rejected, and
- Bids were not always counter offered or forwarded for government technical representative (GTR) approval.

The contracts require each asset manager to prepare and implement a marketing plan that describes how they will meet the performance objectives of the contract. The primary (performance) objectives for the asset managers are to ensure that (1) properties are accurately and competitively valued, (2) sales achieve the highest net return, (3) holding time is minimized, (4) sales create owner-occupant opportunities, and (5) closing proceeds are properly accounted for and delivered to HUD in a timely manner. Each marketing plan contains a price reduction schedule that details the percentage of the appraised value at which properties will

[4] Details on the results of our review for each of the Centers are shown in appendix B (table 3 – Atlanta, table 4 – Denver, table 5 – Philadelphia, and table 6 – Santa Ana).

be listed, the acceptable bid threshold percentages, and the bid threshold percentages that determines when bids will be either counter offered or forwarded for GTR approval. Marketing plans vary for each asset manager depending on factors such as contract/geographic area, etc.

List Prices Were Not Always Reduced in Accordance with Marketing Plans

For 53 of the 120 properties reviewed,[5] the list prices were not reduced according to the price reduction schedules in the asset managers' marketing plan. The marketing plans generally state that properties will be reanalyzed for price reductions after they have been listed on the market from [redacted] and approximately every [redacted] thereafter. While most of the marketing plans state that a review of specified criteria, such as the number of bids received, would be used to determine if a price reduction was warranted, 5 of the 23 marketing plans did not state a review was to be performed and list prices would be reduced according to the price reduction schedules.

Thirty six of the 53 properties should have been reanalyzed for price reductions due to the lack of bid activity. For the 11 properties that had bid activity, the number of bids and bid amount did not justify the asset managers not reducing the list prices according to the price reduction schedules. Therefore, the asset managers should have reduced the list prices for these 47 properties according to the marketing plans. The remaining 6 properties had list prices that were lower than the appropriate percentage of the appraised value (reduced too early). The table below details the number of properties for each Center where the list price was not reduced in accordance with the marketing plans.

Price reductions	Atlanta Center	Denver Center	Philadelphia Center	Santa Ana Center
First price reduction[6]: 45 – 60 days	1	5	5	7
First price reduction[6]: 61 – 90 days	9	1	3	4
First price reduction: over 90 days	1	6	0	0
After first price reduction, subsequent reductions were late according to marketing plans	0	0	3	2
List price lower than marketing plan percentage	1	1	3	1
Total	**12**	**13**	**14**	**14**

For example, we indentified a property that was first listed for sale on April 19, 2011, with the first price reduction occurring almost 3 months later on July 15, 2011 (87 days). According to the asset manager's marketing plan, the property

[5] We determined that the price reductions did not follow the marketing plans only if the list price was not reduced 14 days or more according to the price reduction schedules.
[6] Also included are properties that sold and there was no price reduction.

should have been relisted [redacted] every [redacted]. This property had no bids until it was listed on the market for 91 days and the asset manager did not obtain a broker's price opinion to justify not reducing the list price [redacted]. When the asset manager reduced the price, it did not follow the appropriate percentages in the marketing plan. After 87 days, the list price was [redacted] reduced [redacted]; however, it was reduced 2 days later [redacted] of the appraised value when it should not have been below [redacted].

Only the Philadelphia and Santa Ana Centers had written procedures in place to review the price reductions; however, all of the Centers stated that the asset managers generally reduced the list prices according to their marketing plan. As a result of the asset managers' not reducing list prices according to their marketing plans, properties we reviewed may not have been competitively valued, and the holding time may not have been minimized.

Bids Were Approved That Were Below HUD's Flexible Threshold

For 35 of the 120 properties reviewed,[7] bids were approved that did not meet the flexible net threshold percentages established by HUD. When bids do not meet the minimum acceptable net amount set by the asset managers, they are automatically rejected by the P260 system. The asset managers can then forward these bids to the GTRs for approval, and they may accept bids using flexible thresholds. The flexible thresholds were provided to each Center to follow; however, enforcement was varied and inconsistent, as bids were approved that did not meet the stated thresholds. While HUD provides GTRs the authority to approve bids below the thresholds, there are no defined criteria or procedures detailing how and when this can occur and how it should be documented.

Difference between the flexible threshold and the net bid percentage[7]:	Atlanta Center	Denver Center	Philadelphia Center	Santa Ana Center
Less than 20 percent	0	5	2	2
20-29 percent	5	1	4	0
30-40 percent	4	2	2	0
More than 40 percent	2	0	5	1
Totals	**11**	**8**	**13**	**3**

For example, we identified a property that was listed on the market for 73 days with a bid that was approved [redacted]. According to the asset manager's marketing plan, the bid threshold percentage for 73 days on the market [redacted]. The P260 system initially rejected the bid

[7] For properties with a low list price, we considered the percentage of the gross bid instead of the net bid because in these cases, a bid that met the list price would not meet the bid thresholds because of the minimum realtor commissions.

because it did not meet the minimum acceptable thresholds, and notes in the system stated that the bid was manually approved by HUD because it was aged inventory with no offers. However, [redacted] we identified four previous bids on the property (all within 45 days of the accepted bid). Three of the bids were approximately 200 to 600 percent higher than the approved bid that was eventually accepted.

The Atlanta, Denver, and Philadelphia Centers stated that bids that did not meet the flexible thresholds could be accepted by the GTR based on external factors such as when the property was aged inventory and had no bids. However, the Centers did not have specific national, standardized written procedures in place for accepting bids below the flexible thresholds or defining how many days on the market would be considered aged inventory. As a result of HUD lacking national standardized, specific procedures and approving bids that did not meet the flexible thresholds, the highest net return for properties sold may not have always been achieved.

Bids Were Improperly Rejected

For 21 of the 120 properties reviewed, bids that met the minimum bid threshold percentages were improperly rejected by the P260 system. For these properties, it took an average of 101 days to sell after the first acceptable bid was improperly rejected and on average sold for $2,956[8] less. Some bids were improperly rejected because the P260 system recommended an acceptable bid based only on the threshold percentage of the list price and not the appraised value. Some of the asset managers, specifically at the Santa Ana Center, had threshold percentages based on the list price and appraised value while the asset managers at the other Centers had threshold percentages based only on the list price. In other cases, the correct acceptable bid thresholds from the marketing plans were not entered into the P260 system. As a result of HUD improperly rejecting bids, the highest net return for properties was not always achieved, and the holding time was not minimized (see appendix B, table 1).

Bids Were Not Always Counter Offered or Forwarded for Government Technical Representative Approval

For 36 of 120 properties reviewed, bids that met applicable thresholds were not always counter offered or forwarded to the GTRs for approval. The GTRs do not review bids that are rejected; it is the responsibility of the asset managers to review the bids and forward them to the GTR for approval if they meet the applicable threshold. As a result of the asset managers' not submitting a counter offer or forwarding bids that met certain thresholds to the GTR for approval, the holding time may not have always been minimized.

For example, a bid for a property listed for 171 days was submitted and properly rejected because the net to HUD was below the minimum acceptable amount.

[8] See appendix B, table 1.

However, the bid should have been forwarded to the GTR for approval because it met the threshold percentage for GTR approval. The bid [redacted] of the appraised value ([redacted] percent lower than the acceptable bid threshold), and the threshold percentage for GTR approval [redacted].

Field Service Manager Contracts Were Not Always Enforced

The review of 125 HUD REO properties listed on the market between February and May 2012 across the four Centers identified that the field service managers did not properly maintain properties and conduct routine inspections within the required timeframes. Although the Centers were already aware of these issues, HUD did not implement a quarterly performance report to assign properties to the field service managers based on performance. Instead, it allowed the field service managers to submit voluntary price reductions and, initiated in October of 2011, assigned more properties to field service managers based solely on the price of services, disregarding performance. As a result, more properties may have been assigned to field service managers that had lower prices but were not performing at a satisfactory level. HUD has indicated plans to implement a performance scorecard to uniformly assess the performance of field service managers.

OIG Conducted Property Inspections

We inspected 125 properties in the Atlanta, GA, Kansas City, MO, Los Angeles, CA, Philadelphia, PA, and Phoenix, AZ, areas and determined that 75 properties were not properly maintained. The field service manager contract states that properties must remain in ready-to-show condition until sold; however,

- 42 properties had yards that were not maintained (for example, tall weeds),
- 30 properties were not clean (for example, dirty floors or carpets, trash or debris, dead insects, mold or mildew, and bad odor),
- 23 properties had trash or debris in the yards or front entrance,
- 3 properties had an active water leak,
- 21 properties had broken or unapproved boarded doors or windows,[9] and
- 8 properties were not secure.

[9] According to HUD officials, field service managers are allowed to temporarily board doors and windows only with GTR approval. We determined that the properties identified had boarded doors or windows for an extended period.

Maintenance deficiency	Atlanta Center	Denver Center	Philadelphia Center	Santa Ana Center
Not secure	4	2	1	1
Active water leak	0	3	0	0
Broken or unapproved boarded doors or windows	2	12	5	2
Interior not clean	5	17	4	4
Yard not maintained	14	9	13	6
Trash or debris outside	0	9	7	7

All of the Centers conducted inspections of properties to determine whether they were properly maintained; however, the frequency at which the inspections occurred was inconsistent. For example, the Philadelphia Center inspected properties every quarter while the Denver Center only inspected properties one time each year because of limited travel funds.

Routine Inspections Were Not Conducted in a Timely Manner

For 100 of the 125 properties reviewed, the field service managers did not conduct routine inspections in a timely manner. The field service manager contract states that, at a minimum, the properties must be inspected once every 2 weeks. In some cases, the routine inspections were late by only 1 day, but in other cases, they were late by as many as 33 days. The table below illustrates, by Center, instances identified in which routine inspections were not conducted in a timely manner.

Number of days completed after the previous inspection:	Atlanta Center	Denver Center	Philadelphia Center	Santa Ana Center
15 to 19 days	18	9	8	13
20 to 29 days	10	6	9	18
30 to 39 days	1	0	4	1
40 days or more	0	0	0	3
Total	**29**	**15**	**21**	**35**

Inappropriate Payments Were Made to Field Service Managers

Field service managers were paid a monthly fee even if the required inspections were not conducted and uploaded into the P260 system. During the audit, HUD created a report[10] to identify missed routine inspections that the field service managers were required to perform, issuing letters requesting reimbursement for

[10] HUD created this report on its own, not as a result of our audit.

the routine inspections that were not conducted between June 2011 and February 2012. For example, during this period, one field service manager did not conduct or upload 15,171 of the 36,462 (42 percent) required routine inspections, and HUD requested reimbursement of $3.1 million. HUD has entered into negotiations with field service managers to collect reimbursements for inspections that were required but not performed.

HUD Identified Contractors With Performance Issues

Some of the Centers[11] had already determined that field service managers were not maintaining properties in a ready-to-show condition and conducting routine inspections every 2 weeks. For example, the Santa Ana Center inspected 29 properties in September 2011 and determined that 47 percent were not in "broom-swept" condition and had debris and other health and safety issues. One of the properties inspected on September 27, 2011, had comments such as "filthy, broken window, roaches, and hair in sink," and they noted that the last inspection date by the field service manager was only 2 days earlier. The Center also began reviewing routine inspections in October 2011 and provided the results to the field service manager; however, performance had not improved. The table below illustrates one example of the performance issues noted for one field service manager.

Date of review	Percentage not performed in a timely manner
October 5, 2011	25%
November 8, 2011	65%
November 18, 2011	36%
December 2, 2011	72%
December 22, 2011	51%
January 12, 2012	40%
January 25, 2012	32%

HUD Underpaid M&M III Contractors

HUD underpaid 1 field service manager for 2 months (January and February 2012) and 21 field service managers from June 2011 to January 2012.

Incorrect Management Fees Paid to 21 Field Service Managers

Property management fees were not always paid to 21 field service managers in accordance with their contracts because they were paid based on the date of assignment for properties rather than the actual date of service. HUD officials

[11] The Denver, Philadelphia, and Santa Ana Centers.

stated that the field service managers should be paid based on the actual date of service for property management. Therefore, field service managers that had different property management fees for option year 1 or submitted a voluntary price reduction that was effective October 2011 were not paid the correct amount. We estimated that HUD overpaid 6 field service managers $491,946 and underpaid 15 field service managers $985,582 from June 2011 to January 2012, for a net underpayment to the 21 field service managers of $493,636[12]. HUD officials identified[13] that the fee calculation methodology was incorrect and made the necessary adjustments in February 2012 for future bills.

Underpaid Field Service Manager After Contract Expansion

A field service manager under the jurisdiction of the Santa Ana Center was underpaid for 2 months (January to February 2012) of its contract due to confusion regarding the price of services after a contract transfer and expansion occurred. When the funds for the Santa Ana Center contract were fully expended, the contract for the same contractor with the Atlanta Center was modified to cover the Santa Ana Center's contract. However, HUD incorrectly interpreted the modified contract, which led to the contractors being paid at the base year pricing rather than option year 1 pricing. HUD agreed with us and initiated adjustments to the bills. We estimated that the Santa Ana Center underpaid the field service manager $60,148[14] for the 2 months.

Other Asset Manager Contract Requirements Were Not Met

Asset managers did not always update appraisals every 6 months and did not always perform inspections in a timely manner as required by the asset manager contracts.

Appraisals Were Not Always Updated Timely

For 19 of the 120 properties reviewed, appraisals were not updated every 6 months as required by the asset manager contracts. The asset manager contract states that a new appraisal shall be obtained every six months until the property is sold. Additionally, for 16 of the 19 properties that did not have appraisals updated timely, the asset managers did not obtain a brokers price opinion to ensure that the properties were accurately valued. Even though the Philadelphia and Santa Ana Centers were the only Centers that had written procedures in place

[12] We obtained the property management billing reports from the P260 system to identify properties that were paid incorrect property management fees (HUD-owned vacant and custodial properties) from June 1, 2011 to May 31, 2012. We used this data to calculate an estimated amount that HUD underpaid or overpaid to field service managers. The estimate does not include fees for partial months.
[13] HUD identified this on its own, not as a result of our audit.
[14] We obtained the property management billing reports from the P260 system to identify properties that were paid incorrect amounts from January 1 to February 29, 2012. We used this data to calculate an estimated amount that HUD underpaid the field service manager. The estimate does not include fees for partial months.

to review if appraisals were updated every six months, all of the Centers had properties with appraisals that were not updated as required[15].

Inspections Were Not Always Performed Timely

According to the asset manager contracts, the asset managers are required to conduct three inspections for each property they are assigned. The first required inspection (initial inspection) must be completed no later than 2 days from notification of the field service manager's completion of initial services, and they must upload the inspection report into the P260 system within 2 days after the inspection. The second required inspection (prior-to-list) must be completed before listing properties for sale. The last required inspection (ready-to-close) must be completed no sooner than 5 days before closing.

Inspection	Atlanta Center	Denver Center	Philadelphia Center	Santa Ana Center
Initial inspection				
• Not conducted	0	0	5	0
• Completed 5 days or more after assigned	4	2	5	2
Prior to list inspection				
• Not conducted	3	1	7	0
• Completed after property was listed	2	1	1	0
Ready-to-close inspection				
• Not conducted	5	0	2	1
• Completed 8 days or more before closing	1	1	2	5
Totals	**15**	**5**	**22**	**8**

During the course of the audit, HUD created a report to identify missed required inspections[10]. A letter was sent to the appropriate asset managers requesting reimbursement for the inspections that were not provided between June 2011 and March 2012.

Other Field Service Manger Contract Requirements Were Not Always Met

The field service managers did not always perform property inspections in a timely manner and did not complete health and safety repairs in 1 day as required by the field service manager contracts for 13 properties that had a health and

[15] See appendix B, tables 3 through 6.

safety work notification. After properties are acquired by HUD, the field service managers are required to conduct a comprehensive property inspection and complete the HUD property inspection report, which includes three parts. The first two parts must be uploaded into the P260 system within 2 days of assignment and the third part 5 days later. For 8 of the 125 properties reviewed, the field service managers did not perform the first two parts of the inspection within 4 days or the third part within 8 days.

HUD Lacked Standard Policies and Procedures

HUD did not develop standard quality assurance procedures until two years after the inception of the M&M III program but instead relied on each Homeownership Center to develop its own procedures. According to the asset manager and field service manager contracts, the GTR would monitor contractor performance based on HUD's quality assurance procedures and issue a quarterly performance report. The contracts indicated that performance below a satisfactory level might impact field service managers' assignments.

At the start of the M&M III program, HUD entered into a contract with an oversight monitor to develop procedures to monitor the performance of asset and field service managers; however, the procedures did not meet HUD's needs, and the contract was terminated. Responsibility was, therefore, placed on each Homeownership Center to develop its own procedures. This situation resulted in procedures that were not consistent across the four Centers, increasing risk to the M&M III program. HUD implemented standard asset manager and field service manager monitoring plans on June 1, 2012,[16] and plans to implement a performance scorecard. HUD's policies and procedures should ensure

- Asset managers reduce the list price of properties according to each asset manager's marketing plan, counter offer all bids that meet the counter offer thresholds, forward bids to the GTR that meet close bid thresholds;

- Homeownership Centers follow the flexible net offer threshold and establish procedures for when the GTRs may accept bids below the flexible thresholds; and

- Asset managers update appraisals every six months or modify its asset manager contracts regarding this requirement.

[16] Because the monitoring plans were not implemented until the end of the audit, we did not review the plans to determine whether they were adequate.

Conclusion

The varied and inconsistent procedures developed by each of the four Homeownership Centers were not adequate to ensure that the asset and field service manager contracts were always enforced. This condition occurred because HUD did not develop national standard procedures and did not implement a performance scorecard to assign properties to field service mangers based on performance. As a result, HUD's REO properties may not have always been competitively valued, holding time may not have always been minimized, sales may not have always achieved the highest net return, and properties may have been assigned to contractors that did not perform at a satisfactory level. In addition, we estimated that, between June 2011 and January 2012, HUD underpaid 15 field service managers $985,582, 6 were overpaid $491,946, and 1 was underpaid $60,148 from January to February 2012.

Recommendations

We recommend that the Deputy Assistant Secretary for Single Family Housing:

1A. Develop and implement standardized policies and procedures for the oversight of REO M&M III asset manager and field service manager contracts that apply to all four Homeownership Centers.[17] Procedures should include controls to address the findings as stated in the report.

1B. Develop and implement procedures to ensure that field service managers are paid only for routine inspections that are conducted. Procedures should include a quarterly review of missed inspections and a process to obtain reimbursement from field service managers that do not perform the required inspections.

1C. Develop and implement procedures for the P260 system to ensure that bids meeting the applicable thresholds based on the listed and appraised values are accepted.

1D. Review the P260 system and its related controls to determine what areas, if any, require additional controls to ensure proper oversight of REO M&M III property disposition (such as creating exception reports, etc.).

1E. Finalize and implement the field service manager scorecard to ensure that properties are assigned to contractors based on performance.

1F. Calculate and reimburse or request repayment for the field service managers that were underpaid or overpaid. We estimated that field service

[17] This recommendation is in process. However, the audit did not review the adequacy of the new procedures.

managers were underpaid $1,045,730[18] ($985,582 +60,148[19]) and overpaid $491,946.[20]

1G. Ensure that HUD receives repayment for routine inspections that were not conducted by field service managers between June 2011 and February 2012 and ensure that repayment is received for inspections that were not provided by asset managers between June 2011 and March 2012.

[18] See appendix B, table 2.
[19] See section “Underpaid Field Service Manager After Contract Expansion.”
[20] See appendix B, table 2.

SCOPE AND METHODOLOGY

Our review of asset manager contracts generally covered HUD REO properties that were acquired from August 1, 2010, to January 31, 2012, and our review of field service manager contracts generally covered HUD REO properties that were listed on the market from February 1 to May 31, 2012. We performed our fieldwork from January to July 2012 at the Atlanta, Denver, Philadelphia, and Santa Ana Homeownership Centers.

To accomplish our objectives, we

- Reviewed the performance work statements in the asset manager and field service manager contracts,
- Reviewed the information in the P260 system for each property selected in our samples,
- Reviewed the procedures in place to monitor the performance of asset managers and field service managers at the Homeownership Centers, and
- Interviewed Homeownership Center officials.

We used computer-processed data maintained by HUD in its information systems that provides case level data on single family housing properties and loans (Single Family Data Warehouse) to identify all properties acquired by HUD. We did not rely on these data to reach our conclusions; therefore, we did not assess the reliability of the data.

To determine whether the asset manager contract requirements were met, we selected a nonstatistical sample of 120 properties (30 at each Homeownership Center) that were acquired between August 1, 2010, and January 31, 2012. The sample represented properties from all 23 asset manager contracts. During this period, 138,802 properties were acquired and 104,762 were conveyance type properties that had closed. The sample was selected based on the following factors:

- Properties with an original list price that was lower than the appraised value (approximately 10 for each Center),
- Properties with a low percentage of the sales price to the last list price (approximately 10 for each Center),
- Properties that had a high number of days in HUD's inventory (approximately 10 for each Center), and
- Properties from all asset manager contracts.

To determine whether the field service manager contract requirements were met, we selected a nonstatistical sample of 125 properties that were listed on the market from January 1 to May 31, 2012. From August 1, 2010, to May 31, 2012, 160,665 properties were acquired; however, we selected properties that were listed for sale only by verifying the properties' status in P260.[21]

[21] Two properties were held off market.

The sample was randomly selected based on properties that were listed on the market in the Atlanta, GA, Kansas City, MO, Los Angeles, CA, Philadelphia, PA, and Phoenix, AZ, areas. The sample represented properties from 18 of the 31 field service manager contracts.

To estimate the amount HUD underpaid or overpaid to field service managers, we obtained the property management billing reports from the P260 system and identified properties that were paid incorrect amounts for property management fees (HUD-owned vacant[22] and custodial properties[23]) from June 1, 2011, to May 31, 2012, and January 1 to February 29, 2012. We determined the correct property management fees for these time periods from the field service manager contracts and calculated the estimated amount the field service managers were underpaid or overpaid. We estimated that 15 field service managers were underpaid more than $985,582 from June 2011 to January 2012[24], 6 were overpaid $491,946 from June 2011 to January 2012[24], and 1 was underpaid $60,148 from January to February 2012.[25]

We used computer-processed data maintained in the P260 system. We assessed the reliability of HUD's P260 system data by (1) performing limited testing to determine whether data were supported by reports uploaded into the system, (2) reviewing information about the data and the system that produced them, and (3) interviewing HUD officials knowledgeable about the data. We considered the data to be sufficiently reliable for the purposes of this report.

We conducted the audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

We provided the discussion draft report to HUD on August 10, 2012 and received informal written comments on August 24, 2012. The discussion draft was revised and reissued to HUD on August 30, 2012. Based on the revised discussion draft, HUD declined to provide a formal written response.

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[22] HUD-owned properties are properties that HUD owns by reason of payment of an insurance claim or another acquisition method.

[23] Custodial properties are borrower owned properties that serves as security for a secretary-held mortgages (including a home equity conversion mortgage), which HUD, through the contractor, has taken possession of following default and vacancy or abandonment.

[24] See table 2, appendix B.

[25] The estimate does not include fees for partial months.

INTERNAL CONTROLS

Internal control is a process adopted by those charged with governance and management, designed to provide reasonable assurance about the achievement of the organization's mission, goals, and objectives with regard to

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

Internal controls comprise the plans, policies, methods, and procedures used to meet the organization's mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations as well as the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined that the following internal controls were relevant to our audit objective:

- Policies and procedures intended to ensure that the asset manager and field service manager contract requirements were met (finding 1).

We assessed the relevant controls identified above.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, the reasonable opportunity to prevent, detect, or correct (1) impairments to effectiveness or efficiency of operations, (2) misstatements in financial or performance information, or (3) violations of laws and regulations on a timely basis.

Significant Deficiency

Based on our review, we believe that the following item is a significant deficiency:

- HUD did not implement adequate procedures to ensure consistent and adequate enforcement of REO M&M III asset and field service managers' contracts (finding 1).

APPENDIXES

Appendix A

SCHEDULE OF QUESTIONED COSTS AND FUNDS TO BE PUT TO BETTER USE

Recommendation number	Ineligible 1/	Funds to be put to better use 2/
1F	$491,946	$1,045,730
Total	$491,946	$1,045,730

1/ Ineligible costs are costs charged to a HUD-financed or HUD-insured program or activity that the auditor believes are not allowable by law; contract; or Federal, State, or local policies or regulations. The overpayments to the field service managers are ineligible because HUD paid fees that were in excess of the amounts specified in the field service manager contracts.

2/ Recommendations that funds be put to better use are estimates of amounts that could be used more efficiently if an Office of Inspector General (OIG) recommendation is implemented. These amounts include reductions in outlays, deobligation of funds, withdrawal of interest, costs not incurred by implementing recommended improvements, avoidance of unnecessary expenditures noted in preaward reviews, and any other savings that are specifically identified. If HUD implements our recommendations, it will pay the field service managers the appropriate amounts for services that were provided for HUD REO properties. The costs for these services were agreed to by HUD and are specified in the contract with each field service manager. Funds that should have been obligated and expended for the management and marketing of HUD REO properties will be disbursed as intended, resulting in correct past and future payments. Additionally, identification and payment of underpayments will result in potentially identifying future reimbursement errors and contribute to minimizing the risk to the REO program.

Appendix B

DETAILED RESULTS OF OIG'S REVIEW SAMPLE

Table 1: The table below lists the properties that had bids that met the minimum bid threshold percentages but were improperly rejected by the P260 system.

	Net amount of improperly rejected bid	Date of improperly rejected bid	Net amount of accepted bid	Date of accepted bid	Difference in days	Difference in amount
1	$ 15,157	06/05/2011	$ 7,138	12/19/2011	197	$ (8,019)
2	34,125	01/25/2011	13,100	12/16/2011	325	(21,025)
3	52,722	10/27/2011	48,843	11/28/2011	32	(3,879)
4	139,900	03/01/2011	158,015	03/31/2011	30	18,115
5	155,100	02/02/2011	136,300	04/21/2011	78	(18,800)
6	70,500	09/28/2011	82,800	10/04/2011	6	12,300
7	75,200	03/30/2011	72,346	04/28/2011	29	(2,854)
8	41,300	08/18/2011	49,632	08/26/2011	8	8,332
9	68,150	04/12/2011	31,020	08/03/2011	113	(37,130)
10	38,540	08/09/2011	34,968	12/21/2011	134	(3,572)
11	61,100	08/29/2011	61,425	11/01/2011	64	325
12	95,550	10/17/2011	96,200	10/20/2011	3	650
13	90,804	10/15/2011	109,267	11/18/2011	34	18,463
14	164,700	03/12/2011	154,066	09/22/2011	194	(10,634)
15	56,912	08/22/2011	53,872	11/02/2011	72	(3,040)
16	60,090	01/10/2011	56,420	09/22/2011	255	(3,670)
17	53,486	09/24/2011	46,400	12/27/2011	94	(7,086)
18	136,500	01/06/2011	128,600	10/16/2011	283	(7,900)
19	115,621	02/15/2011	123,140	02/22/2011	8	7,539
20	141,050	03/28/2011	137,417	09/08/2011	164	(3,633)
21	$ 48,230	09/24/2011	$ 51,700	09/25/2011	1	$ 3,470
Average difference					**101**	**$ (2,956)**

Table 2: The table below lists the field service managers that were underpaid or overpaid. We obtained the property management billing reports from the P260 system to identify properties that were paid incorrect amounts for property management fees (HUD-owned vacant and custodial properties) from June 1, 2011, to May 31, 2012. We then this used data to calculate an estimated amount that HUD underpaid field service managers[25].

Field service manager	Area	Amount underpaid or overpaid – custodial properties	Amount underpaid or overpaid – HUD-owned vacant properties	Total amount underpaid or overpaid
Asset Management Specialists	2S	$ 4,032	$ 161,721	$ 165,753
A2Z Field Services	1A	(24,483)	(101,115)	(125,598)
Asset Management Specialists	1A	3,509	85,915	89,424
Innotion Enterprises	1A	775	48,920	49,695
Innotion Enterprises	2A	570	40,788	41,358
CWIS LLC	2A	(158,088)	56,232	(101,856)
PK Management Group	2A	1,779	91,013	92,792
Asset Management Specialists	1P	626	43,740	44,366
Asset Management Specialists	3P	6,307	31,752	38,059
A-Sons Construction	1P	(1,480)	(91,500)	(92,980)
A-Sons Construction	3P	2,871	30,704	33,575
IEI-Tidewater	1P	(5,041)	(29,026)	(34,067)
SIGMA Construction	1P	368	29,055	29,423
A2Z Field Services	2P	(10,994)	(34,622)	(45,616)
Innotion Enterprises	2P	835	34,944	35,779
Asset Management Specialists	1D	367	65,815	66,182
Asset Management Specialists	2D	1,592	82,454	84,046
Asset Management Specialists	3D	1,567	45,688	47,255
SIGMA Construction	1D	2,856	135,418	138,274
A2Z Field Services	2D	(17,738)	(74,091)	(91,829)
First Preston	3D	$ 517	$ 29,084	$ 29,601
Total estimated overpayment				$ (491,946)
Total estimated underpayment				$ 985,582
Net underpayment				**$ 493,636**

Table 3: The table below lists the properties that did not meet the asset manager contract requirements for the Atlanta Homeownership Center.

Case number	List prices not reduced according to marketing plans		Bids approved that were below HUD's flexible threshold (net bid % / days listed)	Bids improperly rejected	Bids not counter-offered or forwarded for GTR approval	Appraisal (days updated late)
	Price reductions	Bid activity[26]				
137-3962417	--	--	--	--	Bid 22	--
501-7209511	--	--	--	--	Bid 6	--
381-4915315	76 days to 1st price reduction	2 bids (75% and 80%)	9% / 153 days	--	--	--
381-8449201	63 days to 1st price reduction	No bids	10% / 144 days	--	--	--
381-7363684	78 days to 1st price reduction	No bids	13% / 153 days	--	--	--
137-1116826	91 days to 1st price reduction	5 bids (19% to 64%)	10% / 170 days	--	Bid 2	--
381-8105401	82 days to 1st price reduction	No bids	15% / 156 days	--	--	--
011-4803882	--	--	28% / 92 days	--	--	--
381-7226514	--	--	30% / 55 days	--	--	--
094-5107146	--	--	37% / 82 days	--	--	--
093-6046741	--	--	39% / 78 days	--	--	--
381-6916841	--	--	40% / 53 days	--	--	--
101-9802695	62 days to 1st price reduction	1 bid (100%)	--	--	Bid 18	--
461-4445387	60 days to 1st price reduction	No bids	--	--	--	--
151-3239001	78 days to 1st price reduction	No bids	26% / 212 days	Bid 14	--	--
381-8167940	62 days to 1st price reduction	7 bids (67% to 102%)[27]	--	--	--	--
101-7976775	4th price reduction 34 days early	n/a – reduced early	--	Bid 2	Bid 3	14 days
011-5022658	72 days to 1st price reduction	No bids	--	--	Bid 5	57 days
137-3201769	--	--	--	--	Bid 2	--
092-9572254	--	--	--	Bid 71	Bid 17	41 days
501-4877077	87 days to 1st price reduction	No bids	--	--	--	42 days
095-0218530	--	--	--	--	Bid 5	--
	12	**12**	**11**	**3**	**9**	**4**

[26] For tables 3, 4, 5, and 6, this column shows the bid activity (and range of gross bid percentages) when the properties should have been reanalyzed for a price reduction.
[27] The marketing plan for this property did not state that a review of specific criteria, such as the number of bids received, would be performed and list prices would be reduced according to the price reduction schedules.

Table 4: The table below lists the properties that did not meet the asset manager contract requirements for the Denver Homeownership Center.

Case number	List prices not reduced according to marketing plans		Bids approved that were below HUD's flexible threshold (net bid % / days listed)	Bids improperly rejected	Bids not counter-offered or forwarded for GTR approval	Appraisal (days updated late)
	Price reductions	Bid activity[26]				
271-9713908	121 days to 1st price reduction	No bids	--	--	--	--
052-3574926	--	--	--	--	Bid 11	--
511-0190358	--	--	--	--	Bid 2	--
492-7579338	--	--	--	--	Bid 7	--
031-3027882	--	--	20% / 198 days	--	--	--
031-3214670	47 days to 1st price reduction	No bids	28% / 120 days	--	--	--
493-8896277	--	--	33% / 248 days	--	--	--
493-8942024	--	--	33% / 126 days	--	--	--
493-8262363	--	--	35% / 198 days	--	--	--
421-3962655	54 days to 1st price reduction	No bids	36% / 129 days	--	--	--
052-4286327	53 days to 1st price reduction	No bids	--	--	--	--
031-3474285	60 days to 1st price reduction	No bids	40% / 227 days	--	--	--
491-8982707	--	--	43% / 143 days	--	--	--
221-3808709	55 days to 1st price reduction	No bids	--	--	--	--
422-2327433	90 days to 1st price reduction	No bids	--	--	--	--
291-3436572	5th price reduction 23 days early	n/a – reduced early	--	--	Bid 1	--
271-7211055	98 days to 1st price reduction	1 bid (40%)	--	--	--	16 days
492-7432845	115 days to 1st price reduction	No bids	--	--	--	--
271-9312888	124 days to 1st price reduction	No bids	--	--	--	211 days
161-2214121	111 days to 1st price reduction	No bids	--	--	--	156 days
495-7803491	91 days to 1st price reduction	No bids	--	--	--	--
492-8472160	--	--	--	--	Bid 6	--
	13	**13**	**8**	**0**	**5**	**3**

Table 5: The table below lists the properties that did not meet the asset manager contract requirements for the Philadelphia Homeownership Center.

Case number	List prices not reduced according to marketing plans		Bids approved that were below HUD's flexible threshold (net bid % / days listed)	Bids improperly rejected	Bids not counter-offered or forwarded for GTR approval	Appraisal (days updated late)
	Price reductions	Bid activity[26]				
442-2278845	--	--	--	--	Bid 5	--
413-4523969	68 days and no price reduction	No bids	--	--	--	--
411-3961061	Reduced to 63% 97 days early	n/a – reduced early	--	--	Bid 6	--
548-4317659	--	--	--	Bid 27	--	--
251-3717332	58 days to 1st price reduction	No bids	--	--	--	85 days
541-8141625	--	--	--	Bid 8	--	--
412-4920866	65 days to 1st price reduction	No bids	1% / 92 days	--	--	--
412-5466643	--	--	1% / 118 days	--	Bid 1	--
412-4885945	84 days to 1st price reduction	4 bids (59% to 85%[27])	1% / 141 days	--	Bid 2	--
261-7445720	--	--	13%[28] / 203 days	--	--	--
263-3952030	46 days to 1st price reduction	No bids	11%[28] / 272 days	--	--	--
441-5796447	--	--	29% / 48 days	--	--	--
412-5328349	--	--	23% / 46 days	--	--	--
262-1049968	--	--	50%[28] / 25 days	--	--	--
541-7197300	1st price reduction 15 days early	n/a – reduced early	36% / 61 days	--	--	--
261-7685738	--	--	50%[28] / 21 days	--	--	--
374-4604362	--	--	--	--	--	--
351-3076167	7th price reduction 71 days late	3 bids (36% to 54%) from 4th price reduction to when the property should have been reanalyzed (to 30%)	--	--	--	--
263-4369457	2nd price reduction 21 days late	14 bids (20% to 53%) from 1st price reduction to when the property should have been reanalyzed	21%[28] / 396 days	--	--	14 days
541-7842042	2nd price reduction 23 days late	No bids	--	--	Bid 5	--
241-7714259	57 days to 1st price reduction	No bids	--	Bid 46	--	--
413-4587929	Reduced to 81% 28 days early	n/a – reduced early	--	--	--	--
261-6272389	54 days to 1st price reduction	3 bids (53% to 79%)	--	--	Bid 21	--
261-8901244	--	--	57%[28] / 119 days	--	--	--
371-3652758	57 days to 1st price reduction	1 bid (58%)	--	--	--	--
411-4088062	--	--	69% / 53 days	--	Bid 40	194 days
	14	**14**	**13**	**3**	**7**	**3**

[28] Gross bid was used because this was a property with a low value.

Table 6: The table below lists the properties that did not meet the asset manager contract requirements for the Santa Ana Homeownership Center.

Case number	List prices not reduced according to marketing plans		Bids approved that were below HUD's flexible threshold (net bid % / days listed)	Bids improperly rejected	Bids not counter-offered or forwarded for GTR approval	Appraisal (days updated late)
	Price reductions	Bid activity[26]				
431-4505103	2nd price reduction 20 days late	No bids	--	Bid 1	--	--
561-8473969	Reduced to 80% 26 days early	n/a – reduced early	--	Bid 7	Bid 11	--
561-8542696	--	--	--	Bid 6	Bid 3	--
197-3528113	--	--	--		Bid 5	--
561-9240749	--	--	--	--	Bid 6	--
048-4741162	87 days to 1st price reduction	No bids	--	Bid 4	Bid 3	--
332-4501285	--	--	--	Bid 1	Bid 7	--
043-7737960	--	--	18% / 73 days	--	Bid 1	--
023-1609905	--	--	--	--	Bid 3	--
023-1783591	--	--	--	--	--	13 days
561-9215977	--	--	42% / 153 days	--	--	--
023-3487331	--	--	--	--	--	11 days
045-6444917	--	--	--	Bid 3	Bid 1	--
023-2781516	49 days to 1st price reduction	No bids	--	--	--	12 days
045-6475779	--	--	54% / 73 days	--	--	--
562-2034593	52 days to 1st price reduction	No bids	--	--	--	
023-2051944	45 days to 1st price reduction	No bids	--	--	--	17 days
332-4518490	65 days to 1st price reduction	No bids	--	Bid 4	Bid 12	--
561-8230978	52 days to 1st price reduction	No bids	--	Bid 3	--	--
048-4548470	--	--	--	Bid 7	--	75 days
561-8560500	2nd price reduction 61 days late	No bids	--	Bid 2	--	--
431-4527167	62 days to 1st price reduction	No bids	--	Bid 5	Bid 4	142 days
022-1931864	54 days to 1st price reduction	No bids	--	Bid 3	Bid 2	17 days
332-4747742	70 days to 1st price reduction	No bids	--	Bid 2	--	--
022-2044309	56 days to 1st price reduction	No bids	--	Bid 3	Bid 2	17 days
048-4736293	60 days to 1st price reduction	2 bids (71% and 100%)	--	Bid 3	Bid 7	--
022-1867868	--	--	--	--	Bid 1	16 days
	14	**14**	**3**	**15**	**15**	**9**