

Audit Report

Department of Housing and Community Development

November 2024

Public Notice

In compliance with the requirements of the State Government Article Section 2-1224(i), of the Annotated Code of Maryland, the Office of Legislative Audits has redacted cybersecurity findings and related auditee responses from this public report.



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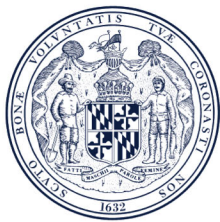
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DEPARTMENT OF LEGISLATIVE SERVICES
OFFICE OF LEGISLATIVE AUDITS
MARYLAND GENERAL ASSEMBLY

Victoria L. Gruber
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Brian S. Tanen, CPA, CFE
Legislative Auditor

November 14, 2024

Senator Clarence K. Lam, M.D., Senate Chair, Joint Audit and Evaluation Committee
Delegate Jared Solomon, House Chair, Joint Audit and Evaluation Committee
Members of Joint Audit and Evaluation Committee
Annapolis, Maryland

Ladies and Gentlemen:

We have conducted a fiscal compliance audit of the Department of Housing and Community Development (DHCD) for the period beginning July 11, 2018 and ending October 31, 2022. DHCD provides services to strengthen communities and provides affordable housing for people of limited income. DHCD also works with partners to finance housing opportunities and revitalize places for Maryland citizens to live, work, and prosper.

Our audit disclosed that DHCD did not effectively monitor recipients of multifamily loans for compliance with the terms of the related agreements. DHCD provides loans to multifamily housing developers for the creation or preservation of affordable rental housing units for low-income individuals. We found that DHCD did not always obtain and review required documentation from loan recipients and physical inspections of loan recipients' properties were not sufficiently documented to ensure that low-income renters met the eligibility requirements specified in the loan agreements.

In addition, DHCD did not adequately follow-up on instances of noncompliance reported by the loan recipients. In this regard, during calendar year 2021, 57 recipients self-reported that they were not in compliance with certain terms of the loan agreements, including age and income requirements. However, DHCD could not readily document that it followed up with the recipients to ensure that the deficiencies were corrected. DHCD also did not take appropriate action when its inspections determined that low-income housing was not being provided in

accordance with the loan agreements, and that significant health and safety concerns identified during inspections were corrected within 24 hours as required.

DHCD did not have an independent review process to ensure that reconciliations of its State-funded housing loans were completed properly and that errors and reconciling items were resolved timely. According to DHCD records, the State-funded loan receivable balance as of June 30, 2022 totaled approximately \$1.07 billion. DHCD also did not establish policies governing the issuance of venture debt loans under the Neighborhood Business Works Program. As of March 2023, DHCD had issued three venture debt loans totaling \$1.5 million.

Our audit also disclosed that DHCD did not comply with State procurement regulations when obtaining marketing services from two vendors and did not monitor services provided by a third vendor to ensure the marketing services were received and amounts invoiced were proper.

Furthermore, our audit disclosed cybersecurity-related findings. However, in accordance with the State Government Article, Section 2-1224(i) of the Annotated Code of Maryland, we have redacted the findings from this audit report. Specifically, State law requires the Office of Legislative Audits to redact cybersecurity findings in a manner consistent with auditing best practices before the report is made available to the public. The term “cybersecurity” is defined in the State Finance and Procurement Article, Section 3.5-301(b), and using our professional judgment we have determined that the redacted findings fall under the referenced definition. The specifics of the cybersecurity findings were previously communicated to those parties responsible for acting on our recommendations.

Finally, our audit included a review to determine the status of the seven findings contained in our preceding audit report. For the non-cybersecurity-related findings, we determined that DHCD satisfactorily addressed three of the five findings. The remaining two findings are repeated in this report.

DHCD’s response to this audit is included as an appendix to this report. We reviewed the response and noted general agreement to our findings and related recommendations. Based on our review of the written responses and additional clarification obtained from DHCD, we believe the corrective actions identified are sufficient to address all audit issues. Consistent with State law, we have redacted the elements of DHCD’s response related to the cybersecurity audit findings. Finally, we have edited DHCD’s response to remove certain vendor names or products, as allowed by our policy.

We wish to acknowledge the cooperation extended to us during the audit by DHCD and its willingness to address the audit issues and implement appropriate corrective actions.

Respectfully submitted,

Brian S. Tanen

Brian S. Tanen, CPA, CFE
Legislative Auditor

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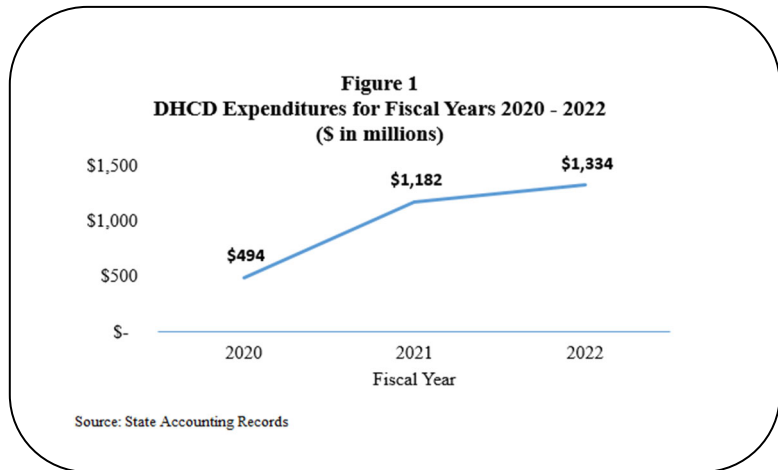
Background Information

Agency Responsibilities

The Department of Housing and Community Development (DHCD) provides services to strengthen communities and provides affordable housing for people of limited income. DHCD's three operating divisions (Development Finance, Credit Assurance, and Neighborhood Revitalization) administer various housing and neighborhood revitalization programs that assist families with affordable homeownership, foreclosure prevention counseling, affordable rental housing, and housing rehabilitation needs. Through these housing programs, DHCD provides loans and grants for the purchase and/or rehabilitation of single-family homes and for the acquisition, construction, renovation, and/or rehabilitation of multifamily rental housing and community development institutions. DHCD's remaining divisions provide administrative support to assist in achieving its goals.

As shown in Figure 1, DHCD's expenditures have increased significantly since fiscal year 2020, primarily because of the COVID-19 public health emergency.¹

Specifically, DHCD was responsible for administering more than \$2 billion in State and federal COVID-19 funds through various programs such as the Emergency Rental Assistance Program and the Maryland Homeowners Assistance Fund.



According to the State's records, during fiscal year 2022, DHCD's expenditures totaled approximately \$1.3 billion (see Figure 2 on the following page), of which \$1.1 billion related to loans and grants for the various programs DHCD administers. DHCD's programs are funded by a combination of revenue bonds that it issues, Federal Funds, and State appropriations.

¹ Total expenditures in Figure 1 and Figure 2 do not agree because Figure 1 includes non-budgeted funds.

Figure 2
DHCD Positions, Expenditures, and Funding Sources

Full-Time Equivalent Positions as of June 30, 2022		
	Positions	Percent
Filled	305	91.6%
Vacant	28	8.4%
Total	333	
Fiscal Year 2022 Expenditures		
	Expenditures	Percent
Salaries, Wages and Fringe Benefits	\$ 41,258,643	3.1%
Technical and Special Fees	6,433,922	0.5%
Operating Expenses	1,265,765,533	96.4%
Total	\$1,313,458,098	
Fiscal Year 2022 Funding Sources		
	Funding	Percent
General Fund	\$ 40,037,023	3.0%
Special Fund	120,654,229	9.2%
Federal Fund	1,123,719,545	85.6%
Reimbursable Fund	29,047,301	2.2%
Total	\$1,313,458,098	

Source: State financial and personnel records

Financial Statement Audits

For fiscal years 2019 through 2022, DHCD engaged independent certified public accounting firms to perform audits of certain of its financial activities, including its revenue bonds. Based on significance and risk, we reviewed the following financial statements:

- Community Development Administration (CDA) Single Family Housing Revenue Bonds
- CDA Revenue Obligation Funds
- CDA Multifamily Mortgage Revenue Bonds
- State-Funded Loan Programs

In the related audit reports, the firms stated that the financial statements presented fairly, in all material respects, the related financial positions and the changes in net assets and cash flows related to the aforementioned programs for the years then ended in accordance with accounting principles generally accepted in the United States of America.

According to its audited financial statements, as of June 30, 2022, DHCD had loans outstanding (net of allowances for loan losses totaling \$363.1 million) totaling approximately \$1.71 billion (see Figure 3).

Figure 3
Loans Outstanding as of June 30, 2022 (in millions)

Loan Program	Funding Source		Total Loans Receivable	
	State Funds	Revenue Bonds	Amount	Percentage
Single Family	\$122	\$464	\$586	34.3%
Multifamily	490	360	850	49.8%
Other	96	176	272	15.9%
Total	\$708	\$1,000	\$1,708	

Source: DHCD Audited Financial Statements

Organizational Change

Chapter 74, Laws of Maryland 2021, effective April 13, 2021, transferred the Office of Rural Broadband from the Department of Information Technology to DHCD and renamed it as the Office of Statewide Broadband. The activities of the Office since April 13, 2021 were included in the scope of our current DHCD audit.

Status of Findings From Preceding Audit Report

Our audit included a review to determine the status of the seven findings contained in our preceding audit report dated July 10, 2020. As disclosed in Figure 4 on the following page, for the non-cybersecurity-related findings, we determined that DHCD satisfactorily addressed three of the five findings. The remaining two findings are repeated in this report.

**Figure 4
Status of Preceding Findings**

Preceding Finding	Finding Description	Implementation Status
Finding 1	The Department of Housing and Community Development (DHCD) did not always adhere to State procurement regulations. DHCD also awarded two contracts for amounts substantially higher than the related proposals.	Not repeated
Finding 2	DHCD improperly used marketing and construction management services contracts to obtain goods and services that were outside the scope of the contracts. Certain of these purchases appeared questionable, and DHCD could not document that these goods and services were received.	Not repeated
Finding 3	DHCD's procedures for reconciling the receivable balances for State-funded loans did not ensure that reconciling items were resolved in a timely manner.	Repeated (Current Finding 3)
Finding 4	DHCD did not monitor multifamily housing loans timely and effectively. In addition, DHCD did not always take appropriate action when a loan recipient did not comply with the loan agreement.	Repeated (Current Finding 1)
Finding 5	DHCD did not ensure multifamily housing loans were recorded in its automated loan servicing system used for the collection of loan repayments. In addition, for certain of these loans, DHCD did not generate timely and accurate annual invoices and pursue delinquent accounts.	Not repeated
Finding 6	Sensitive personally identifiable information maintained by DHCD was stored without adequate safeguards.	Status Redacted ²
Finding 7	Malware protection controls for DHCD computers were not sufficient to provide adequate assurance that computers were properly protected from security risks.	Status Redacted ²

² Specific information on the current status of this cybersecurity-related finding has been redacted from the publicly available report in accordance with State Government Article, Section 2-1224(i) of the Annotated Code of Maryland.

Findings and Recommendations

Multifamily Housing Program

Background

DHCD provides loans to multifamily housing developers for the creation or preservation of affordable rental housing units for low-income individuals. State law and the financing agreements require that a portion of the rental units in each multifamily housing project that receives DHCD financing be reserved for low-income households for the greater of 15 years or the number of years required by federal law (if the project also receives federal assistance). In addition, the loan recipients (developers) are required to maintain the facilities in accordance with certain pre-established standards.

Different divisions within DHCD are responsible for various aspects of the multifamily housing program, including loan underwriting, monitoring compliance, and collection. DHCD uses one automated system to monitor compliance with the terms of the financing (loan) agreements (the loan monitoring system) and a second automated system to generate invoices and track loan activity such as repayments (the loan servicing system). The amount and timing of loan repayments vary based on the type of loan.

Once construction is complete, recipients are required to submit an Annual Certificate of Compliance (ACC) certifying that the facility is in compliance with the tenant income restrictions specified in the loan agreement, and that all units are suitable for occupancy. The recipient is also required to maintain sufficient records supporting the report for subsequent inspection by DHCD. DHCD performs annual onsite inspections of the facilities to ensure that information reported in the ACC is accurate and that housing conditions meet DHCD standards, including being safe and sanitary. According to agency records, DHCD was responsible for monitoring 609 facilities that were recipients of multifamily housing loans during calendar year 2021.

Finding 1**DHCD did not effectively monitor recipients of multifamily loans for compliance with the terms of the loan agreements.****Analysis**

DHCD did not effectively monitor recipients of multifamily loans for compliance with the terms of the loan agreements.

- DHCD did not obtain and review ACCs from all multifamily loan recipients. Specifically, as of April 2023, DHCD had not obtained ACCs for 9 of the 609 loan recipients for calendar year 2021 (which were due in June 2022) and had not reviewed 68 other ACCs. As a result, DHCD lacked assurance that the approximately 4,900 residential units provided by these 77 recipients were compliant with the terms of the loan agreements. DHCD advised that it was not always able to obtain and review the ACCs timely due to high turnover of inspection staff.
- Annual physical inspections of loan recipient properties did not sufficiently document that low-income renters met the eligibility requirements specified in the loan agreements. DHCD procedures required inspectors to verify that low-income renters met the eligibility requirements but did not specify what records were to be reviewed or how the review was to be documented. Our review of inspection results on file for 20 projects with 2,075 rental units, valued at \$127.6 million, disclosed that DHCD did not retain any documentation to support the verification of renter eligibility. A similar condition was commented upon in our preceding audit report. DHCD's response to that report indicated that it would update its procedures to address the specific documents to review by September 2019. However, as of April 2023, DHCD had not updated the procedures.
- DHCD did not adequately follow up on instances of noncompliance reported by the loan recipients. Our review disclosed that 57 (11 percent) of the 532 ACCs that DHCD reviewed for calendar year 2021 indicated that the recipients were not in compliance with certain terms of the loan agreements such as age and income requirements. For example, one recipient of a \$4.2 million loan reported that one-third of its low-income housing units were occupied by individuals who exceeded the income limits specified in the loan agreement. DHCD could not readily document that it followed up with the 57 non-compliant loan recipients to ensure that the deficiencies were corrected³

³ The loan agreements provide that tenants who exceed the specified income limit must vacate the unit within 24 months.

or to demand repayment of the loan proceeds and/or accelerate repayment of the loan.

- DHCD did not take appropriate action when its inspections determined that recipients of multifamily housing loans were not providing low-income housing in accordance with the related loan agreements. During our audit testing of various aspects of DHCD's loan monitoring, we identified 3 DHCD inspections for which low-income housing was not provided as required. Specifically, DHCD inspections of 3 loan recipients that provided 56 housing units determined that 39 units had not been used for low-income housing as required, including certain units that had been unoccupied for 8 years as of April 2023. However, as of April 2023, DHCD had not requested repayment of these three loan recipients as permitted by the related agreements. State regulations and the regulatory agreements attached to each loan outline the specific timing of steps for DHCD to demand repayment of the loan proceeds and/or accelerate repayment in the event the borrower fails to comply with income and use restrictions.

A similar condition was noted in our preceding report. DHCD's response to that report indicated that it established a committee to determine the appropriate course of action for noncompliant projects. However, DHCD could not document that the aforementioned three loans were reviewed by this committee and, as of April 2023, did not have a formal plan to ensure that the required amount of low-income housing was provided by these recipients.

Recommendation 1

We recommend that DHCD

- a. obtain and review ACCs for all multifamily loan recipients;**
- b. enhance its inspection procedures to specify the records to be used for verifying renter income eligibility and how this review is to be documented (repeat); and**
- c. take appropriate action when noncompliance is reported by loan recipients and/or identified during the inspections, including for the properties noted above (repeat).**

Finding 2**DHCD did not ensure that significant health and safety concerns identified at multifamily housing facilities were corrected within 24 hours as required.****Analysis**

DHCD did not ensure that significant health and safety concerns identified during its inspections of multifamily facilities were corrected within 24 hours as required. DHCD conducts annual inspections of multifamily housing facilities to ensure the facilities comply with the safety and sanitary requirements of the loan agreements. Loan recipients are required to remedy significant health and safety concerns (such as, the presence of mold, rodents, and missing or damaged safety equipment) identified during these inspections within 24 hours. According to agency records, DHCD inspections conducted during calendar year 2022 identified 468 significant health or safety concerns.

Although inspection results were recorded in a centralized database, DHCD did not have a comprehensive process to track the resolution of significant health and safety concerns to ensure that they were ultimately resolved. Our review of 12⁴ facility inspections conducted between March 2022 and March 2023 disclosed that the inspectors did not follow up to ensure that the health and safety concerns were resolved until 3 to 11 months after the conditions were identified, including 2 conditions that were not followed up on until we brought the matter to DHCD's attention.

For example, one inspection reviewed was conducted in May 2022 and identified that smoke detectors were not installed as required, but DHCD did not verify the condition was corrected until April 2023. Although the inspectors ultimately followed-up on the aforementioned conditions, a comprehensive process to track the resolution of health and safety concerns identified during inspections is critical to ensure that these conditions are addressed within 24 hours as required.

Recommendation 2**We recommend that DHCD develop procedures to ensure that significant health and safety conditions identified at multifamily housing facilities are corrected within 24 hours, as required.**

⁴ We arbitrarily selected 12 inspections from a report of significant inspection concerns between January 2021- March 2023.

State-Funded Loans

Finding 3

DHCD did not have an independent review process to ensure that reconciliations of its State-funded housing loans were completed properly and that errors and reconciling items were resolved timely.

Analysis

DHCD did not have an independent review process to ensure that reconciliations of its State-funded housing loans were completed properly, and that errors and reconciling items were resolved timely. DHCD contracts with loan servicers to administer these loans. DHCD maintains independent internal loan records and records the loans in the State's Financial Management Information System (FMIS). According to State accounting records, the State-funded loan receivable balance as of June 30, 2022 totaled \$1.07 billion,⁵ of which \$847.8 million were administered by one loan servicer. DHCD performs monthly reconciliations of the loan activity recorded in FMIS, DHCD records, and the loan servicers' records to ensure that all loan activity was properly accounted for.

We reviewed DHCD's procedures for reconciling the records related to this loan servicer and found that there was no supervisory review of the reconciliations. As a result, errors and reconciling items were not resolved timely. For example, our review disclosed that the June 30, 2022 reconciliation performed for one loan program administered by this loan servicer did not identify a \$1.3 million discrepancy between DHCD's internal records and FMIS. Our review also disclosed that the reconciliations included 207 reconciling items totaling \$72.5 million that had been unresolved for periods ranging from 6 months to 10 years. For example, the June 30, 2022 reconciliation for one loan program disclosed a \$1.3 million loan issued in December 2020 that was not recorded in FMIS as of June 2022.

Similar conditions regarding DHCD's procedures for reconciling the loan activity and resolving reconciling items in a timely manner have been commented upon in our two preceding audit reports dating back to November 2016. Specifically, our prior report noted that although supervisory employees approved these reconciliations, they did not verify that longstanding reconciling items were resolved. In its response to our prior report, DHCD advised that it would establish procedures to ensure reconciling items were resolved in a timely manner by the end of calendar year 2020. However, our current audit disclosed that

⁵ This amount does not include allowances for loan losses, whereas the total loans outstanding reflected in Figure 3 reflected an allowance for loan losses totaling \$363.1 million.

DHCD discontinued the aforementioned supervisory reviews which precluded DHCD from timely detecting and resolving reconciling items.

Recommendation 3

We recommend that DHCD

- a. ensure that comprehensive independent supervisory reviews of loan record reconciliations are performed; and**
- b. verify that reconciling items, including the differences noted above, are investigated and resolved in a timely manner (repeat).**

Finding 4

DHCD did not establish policies governing the issuance of Neighborhood Business Works venture debt loans.

Analysis

DHCD did not establish policies governing the issuance of Neighborhood Business Works (NBW) venture debt loans. NBW is a small business financing program that provides financial assistance to qualified entities located in Maryland. In calendar year 2019, DHCD began issuing venture debt loans through the NBW program. Venture debt loans are loans made to companies that do not have positive cash flows or significant assets to give as collateral. Venture debt loans typically incorporate the right for the lender (DHCD) to obtain equity in the borrower to compensate for the higher risk of default. According to DHCD records, NBW loans outstanding as of March 2023 totaled \$50.7 million, including three venture debt loans totaling \$1.5 million.⁶

Although DHCD had comprehensive policies for the standard NBW loan process, similar policies were not in place for venture debt loans. Specifically, DHCD policy did not address key elements of the venture debt loan process, including public solicitation and award of loans; conflict of interest prohibitions; and guidance for establishing the loan amount, term, and collateral requirements. The lack of comprehensive policies is significant given that the award process and structure of the venture debt loans differed from other NBW loans.

In this regard, our review disclosed that DHCD did not publicly advertise the availability of venture debt funds and did not require the recipients to submit

⁶ Specifically, DHCD issued a \$500,000 loan to a biopharmaceutical company to provide working capital to expand its manufacturing operation in Maryland and two \$500,000 loans to an animated film production company. An analysis of the loan to the biopharmaceutical company was included in a February 2024 report issued by the Department of Legislative Services' Office of Program Evaluation and Government Accountability entitled *Evaluation of Neighborhood Business Works*.

formal loan applications (including conflict of interest attestations), provide collateral, or demonstrate creditworthiness, as required by DHCD policy for other NBW loans. In addition, the venture debt loans deferred repayment for between 7 to 15 years; while DHCD policy provided for discretion in determining repayment periods, other NBW loans we reviewed generally required borrowers to begin repayment within a few months of the loan execution date.

Recommendation 4

We recommend that DHCD establish comprehensive policies governing the issuance of NBW venture debt loans.

Procurements and Disbursements

Finding 5

DHCD did not comply with State procurement regulations when obtaining marketing services from two vendors and did not monitor services provided by a third vendor to ensure the marketing services were received and amounts invoiced were proper.

Analysis

DHCD did not comply with State procurement regulations when obtaining marketing services from two vendors and did not monitor services provided by a third vendor to ensure the marketing services were received and amounts invoiced were proper. According to the State's accounting records, during the period from July 1, 2018 to June 30, 2022, marketing expenditures totaled approximately \$2.9 million. We tested DHCD's procurement and monitoring of 3 judgmentally selected marketing contracts (based on considerations, such as, materiality) totaling approximately \$2 million and noted the following conditions.

DHCD Did Not Comply with State Procurement Regulations

DHCD did not comply with State procurement regulations when procuring marketing services from two vendors totaling \$552,000 and \$340,000.

Specifically, DHCD did not competitively procure the services and did not enter into formal written agreements with either vendor. In addition, DHCD did not obtain required approvals from the Department of General Services (DGS) and the Board of Public Works (BPW) for either contract.

State procurement regulations require that agencies enter into a competitive procurement and include certain standard contract provisions (such as, delivery and acceptance and termination conditions) for procurements exceeding \$15,000. In addition, procurements for goods or services of \$50,000 or more require

approval from DGS and procurements of \$200,000 or more require approval from BPW.

DHCD advised that it did not comply with the State procurement regulations because these services were provided under the DHCD Sponsorship Program.⁷ However, Sponsorship Program procurements are not exempt from the provisions of State procurement regulations. Furthermore, these contracts would not qualify for the Sponsorship Program because DHCD policy prohibited payments to a vendor under this program in excess of \$15,000.

DHCD Did Not Ensure Certain Marketing Services Were Received and Payments Were Proper

DHCD did not monitor a \$1.1 million marketing contract to ensure services were provided and amounts invoiced were proper. The contract provided that the vendor was to be paid a fixed fee for each advertisement campaign and any media purchases (such as print and digital advertisements) were to be billed as a pass-through to DHCD.

We tested the three highest invoices totaling approximately \$326,000 (consisting of \$294,000 for reimbursable media purchases and \$32,000 for the vendor's fee) for services rendered between June 2021 and August 2022. Our test disclosed that DHCD only verified the propriety of the vendor's fee but did not obtain support for amounts billed for media purchases. DHCD could also not document that it verified the related advertisements were received. Due to the lack of available documentation, we could not determine if the marketing services paid for were received or if the amounts invoiced on this contract were proper.

Recommendation 5

We recommend that DHCD ensure marketing contracts are procured in accordance with State regulations and are properly monitored. Specifically, we recommend that DHCD

- a. competitively solicit all services over \$15,000,**
- b. execute formal written agreements with vendors as required,**
- c. obtain required control agency approval for future contracts and retroactive approval for the contracts above, and**
- d. ensure services are received and the related billings are adequately supported and in accordance with the contract terms prior to payment.**

⁷ DHCD contributes funds, materials, or services to vendors in return for recognition, acknowledgment, or other promotional consideration.

Information Systems Security and Control

We determined that the Information Systems Security and Control section, including Findings 6 through 8 related to “cybersecurity,” as defined by the State Finance and Procurement Article, Section 3.5-301(b) of the Annotated Code of Maryland, and therefore are subject to redaction from the publicly available audit report in accordance with the State Government Article 2-1224(i). Consequently, the specifics of the following findings, including the analysis, related recommendations, along with DHCD’s responses, have been redacted from this report copy.

Finding 6
Redacted cybersecurity-related finding.

Finding 7
Redacted cybersecurity-related finding.

Finding 8
Redacted cybersecurity-related finding.

Audit Scope, Objectives, and Methodology

We have conducted a fiscal compliance audit of the Department of Housing and Community Development (DHCD) for the period beginning July 11, 2018 and ending October 31, 2022. The audit was conducted 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 objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

As prescribed by the State Government Article, Section 2-1221 of the Annotated Code of Maryland, the objectives of this audit were to examine DHCD's financial transactions, records, and internal control, and to evaluate its compliance with applicable State laws, rules, and regulations.

In planning and conducting our audit, we focused on the major financial-related areas of operations based on assessments of significance and risk. The areas addressed by the audit included procurements and disbursements, payroll, certain State-funded loan program transactions, specific programs (such as multifamily and single family housing grants and loans) used by DHCD to promote housing opportunities and revitalize localities throughout the State, and information systems security and control. We also determined the status of the findings included in our preceding audit report.

Our audit did not include an evaluation of internal controls over compliance with federal laws and regulations for federal financial assistance programs (such as Section 8 Housing) and an assessment of DHCD's compliance with those laws and regulations because the State of Maryland engages an independent accounting firm to annually audit such programs administered by State agencies, including DHCD.

Our assessment of internal controls was based on the DHCD's procedures and controls in place at the time of our fieldwork. Our tests of transactions and other auditing procedures were generally focused on the transactions occurring during our audit period of July 11, 2018 to October 31, 2022, but may include transactions before or after this period as we considered necessary to achieve our audit objectives.

To accomplish our audit objectives, our audit procedures included inquiries of appropriate personnel, inspections of documents and records, tests of transactions, and to the extent practicable, observations of the DHCD's operations. Generally,

transactions were selected for testing based on auditor judgment, which primarily considers risk, the timing or dollar amount of the transaction, or the significance of the transaction to the area of operation reviewed. As a matter of course, we do not normally use sampling in our tests, so unless otherwise specifically indicated, neither statistical nor non-statistical audit sampling was used to select the transactions tested. Therefore, unless sampling is specifically indicated in a finding, the results from any tests conducted or disclosed by us cannot be used to project those results to the entire population from which the test items were selected.

We also performed various data extracts of pertinent information from the State's Financial Management Information System (such as revenue and expenditure data) and the State's Central Payroll Bureau (payroll data). The extracts are performed as part of ongoing internal processes established by the Office of Legislative Audits and were subject to various tests to determine data reliability. We determined that the data extracted from these sources were sufficiently reliable for the purposes the data were used during this audit.

We also extracted data from DHCD's project and loan accounting systems for the purpose of testing single and multifamily loans, construction, and weatherization projects. We performed various tests of the relevant data and determined that the data were sufficiently reliable for the purposes the data were used during the audit. Finally, we performed other auditing procedures that we considered necessary to achieve our audit objectives. The reliability of data used in this report for background or informational purposes was not assessed.

DHCD's management is responsible for establishing and maintaining effective internal control. Internal control is a process designed to provide reasonable assurance that objectives pertaining to the reliability of financial records; effectiveness and efficiency of operations, including safeguarding of assets; and compliance with applicable laws, rules, and regulations are achieved. As provided in *Government Auditing Standards*, there are five components of internal control: control environment, risk assessment, control activities, information and communication, and monitoring. Each of the five components, when significant to the audit objectives, and as applicable to DHCD, were considered by us during the course of this audit.

Because of inherent limitations in internal control, errors or fraud may nevertheless occur and not be detected. Also, projections of any evaluation of internal control to future periods are subject to the risk that conditions may change or compliance with policies and procedures may deteriorate.

Our reports are designed to assist the Maryland General Assembly in exercising its legislative oversight function and to provide constructive recommendations for improving State operations. As a result, our reports generally do not address activities we reviewed that are functioning properly.

This report includes findings relating to conditions that we consider to be significant deficiencies in the design or operation of internal control that could adversely affect the DHCD's ability to maintain reliable financial records, operate effectively and efficiently, and/or comply with applicable laws, rules, and regulations. Our report also includes findings regarding significant instances of noncompliance with applicable laws, rules, or regulations. Other less significant findings were communicated to DHCD that did not warrant inclusion in this report.

State Government Article Section 2-1224(i) requires that we redact in a manner consistent with auditing best practices any cybersecurity findings before a report is made available to the public. This results in the issuance of two different versions of an audit report that contains cybersecurity findings – a redacted version for the public and an unredacted version for government officials responsible for acting on our audit recommendations.

The State Finance and Procurement Article, Section 3.5-301(b), states that cybersecurity is defined as “processes or capabilities wherein systems, communications, and information are protected and defended against damage, unauthorized use or modification, and exploitation.” Based on that definition, and in our professional judgment, we concluded that certain findings in this report fall under that definition. Consequently, for the publicly available audit report all specifics as to the nature of cybersecurity findings and required corrective actions have been redacted. We have determined that such aforementioned practices, and government auditing standards, support the redaction of this information from the public audit report. The specifics of these cybersecurity findings have been communicated to DHCD and those parties responsible for acting on our recommendations in an unredacted audit report.

DHCD's response to our findings and recommendations is included as an appendix to this report. Depending on the version of the audit report, responses to any cybersecurity findings may be redacted in accordance with State law. As prescribed in the State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise DHCD regarding the results of our review of its response.

APPENDIX



WES MOORE
Governor
ARUNA MILLER
Lt. Governor
JACOB R. DAY
Secretary
JULIA GLANZ
Deputy Secretary

November 6, 2024

Mr. Brian S. Tanen, CPA, CFE
Legislative Auditor
Office of Legislative Audits
The Warehouse at Camden Yards
351 West Camden Street, Suite 400
Baltimore, MD 21201

Dear Mr. Tanen:

Enclosed, please find the responses to the draft audit report on the Maryland Department of Housing and Community Development for the period beginning July 11, 2018, to October 31, 2022.

If you have any questions, please contact Charles Akoyo at 410-591-4234 or email at charles.akoyo@maryland.gov

Sincerely,

Signed by:

A handwritten signature in black ink, appearing to read "A R Day". The signature is enclosed in a blue rectangular box. Below the signature, the text "6BD3B998912B440..." is visible, followed by the printed name "Jacob R. Day".

Secretary



MARYLAND DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT
7800 HARKINS RD • LANHAM, MD 20706 • DHCD.MARYLAND.GOV
301-429-7400 • 1-800-756-0119 • TTY/RELAY 711 or 1-800-735-2258



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Multifamily Housing Program

Finding 1

DHCD did not effectively monitor recipients of multifamily loans for compliance with the terms of the loan agreements.

We recommend that DHCD

- a. obtain and review ACCs for all multifamily loan recipients;**
- b. enhance its inspection procedures to specify the records to be used for verifying renter income eligibility and how this review is to be documented (repeat); and**
- c. take appropriate action when noncompliance is reported by loan recipients and/or identified during the inspections, including for the properties noted above (repeat).**

Agency Response	
Analysis	
Please provide additional comments as deemed necessary.	<p>DHCD's responses to the specific bulleted sub findings and recommendations are below. In general, DHCD acknowledges the accuracy of the findings and recognizes the need for greater controls for asset management monitoring and compliance operations in the multifamily unit of the Division of Credit Assurance (DCA). While turnover and understaffing were issues that contribute to this finding, they are not the only causes.</p> <p>DCA has begun significant efforts to address these issues, including -</p> <p>A. hiring a new Director and Deputy Director of the Division of Credit Assurance (DCA) in 2023.</p> <p>B. working to expand the quality and quantity of MF staff through hiring and restructuring of positions and responsibilities. Most notably, the MF unit created two new positions - a Deputy Director of Compliance and Quality Control and a Workout Manager - in order to address "Special Assets" - i.e. loans identified as underperforming, at risk or in default - and ensure appropriate policies and procedures are in place, followed and reviewed periodically.</p> <p>C. undertaking a comprehensive review of all multifamily asset management policies and procedures and replacing or creating policies and procedures to provide clarity and direct procedures with specific timelines and delegations of responsibility to MF staff; and</p>

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	<p>D. procuring a new compliance management software system that will provide greater visibility over staff performance and tracking of outcomes. The new compliance system is expected to “go live” prior to 12/31/2025. Each of these efforts will result in significant improvements in the areas where findings have been identified.</p>		
Recommendation 1a	Agree	Estimated Completion Date:	12/31/2024
Please provide details of corrective action or explain disagreement.	<p>DCA leadership has also identified and is prioritizing the lack of policy, structure and sufficient systems to support monitoring and ensure compliance with internal policies for collecting and reviewing ACCs and identifying and escalating issues of non-compliance. These are being addressed in the policies and procedures being reviewed, developed and modified by current management and staff. DHCD will strive for 100% compliance in its loan recipients, but some non-compliance is to be expected. More importantly, DHCD intends to focus on ensuring that it is able to quickly and accurately identify areas of non-compliance and ensure that they are being addressed and resolved.</p>		
Recommendation 1b	Agree	Estimated Completion Date:	12/31/2025
Please provide details of corrective action or explain disagreement.	<p>The existing DCA policies and procedures manual has not been updated, but there has been work completed, both prior to and since the audit, to develop standard forms for file and lease inspections. Renter eligibility is also confirmed, in part, through receipt of annual certificates of compliance and reviews, however DCA acknowledges that each of these procedures needs to be developed and modified and that those have been identified as high priority items for drafting and implementation. DCA will enhance its inspection procedures, including lists of specific documents to review and documentation of those reviews. Drafting of policy and procedure updates to address these issues is underway and will be complete by March 1, 2025, and will continue to be enhanced through implementation and use of the new software system beginning in 2026.</p>		
Recommendation 1c	Agree	Estimated Completion Date:	12/31/2024
Please provide details of corrective action or explain disagreement.	<p>DCA is currently in active system and process development with a vendor for a new compliance software for its multifamily loan programs. This software will provide a robust, commercial off the shelf system for compliance monitoring and exceptions reporting that will assist multifamily staff and management in identifying noncompliance and ensuring it is being addressed.</p> <p>The Special Assets group is tasked with assisting portfolio managers with addressing noncompliance and, in the event the noncompliance is not addressed, and the project is identified as a Special Asset, developing a plan of action and ensuring the resolution and return to standard</p>		

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	<p>servicing or escalation and potential enforcement for non-compliant projects.</p> <p>Each of the compliance issues and defaults for the three loans identified by the auditors have been resolved or are in the special assets' portfolio and active negotiations for workout or enforcement action in consultation with the Office of the Attorney General.</p>
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Finding 2

DHCD did not ensure that significant health and safety concerns identified at multifamily housing facilities were corrected within 24 hours as required.

We recommend that DHCD develop procedures to ensure that significant health and safety conditions identified at multifamily housing facilities are corrected within 24 hours, as required.

Agency Response			
Analysis			
	Agree	Estimated Completion Date:	12/31/2024
Please provide additional comments as deemed necessary.	<p>DHCD recognizes the gap in ensuring monitoring deficiencies are resolved satisfactorily. The existing policies and procedures do not contain specific, mandated processes to ensure “unsatisfactory” or “below average” physical inspections are advanced for further action, nor did DCA have sufficient resources to deal with projects that failed to meet expectations.</p> <p>DHCD agrees with this recommendation. DCA has been and is addressing these findings in the following ways. (1) Development of the Special Assets team and processes for monitoring and resolving projects and loans designated as Special Assets. (2) Projects receiving life, safety and health findings that are not addressed within the required time period will be required to receive a “below average” or “unsatisfactory” designation, and will be unable to be passed, closed or scheduled for future years inspections. Instead, they will be designated as Special Assets and moved to the Department’s Special Assets team for a plan of action and enhanced monitoring until such time as the issues have been resolved. The Department’s policies and procedures are being updated and will reflect these changes. (3) The asset management compliance software will automatically flag projects that receive below average or other designations reflecting high risk and will be able to automatically notify and provide reports to immediate supervisors and Division management. These reports will be reviewed periodically to ensure all outstanding matters are resolved, are being addressed subject to a plan of action, or are moved to active workout or enforcement. DCA expects to develop further processes and procedures through the new compliance software to better track, with specific dates, the successful resolution of identified life, safety and health issues. As such, these procedures will ensure data is inputted tracking whether life, safety and health findings (a) were corrected within 24 hours and, if not, (b) if and when they were corrected. Failures of projects to address findings in a timely manner and/or failures of DCA</p>		

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	staff to follow up and document resolution of these findings, will be tracked in a central system and will result in escalation to management.
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State-Funded Loans

Finding 3
DHCD did not have an independent review process to ensure that reconciliations of its State-funded housing loans were completed properly and that errors and reconciling items were resolved timely.

We recommend that DHCD

- a. ensure that comprehensive independent supervisory reviews of loan record reconciliations are performed; and**
- b. verify that reconciling items, including the differences noted above, are investigated and resolved in a timely manner (repeat).**

Agency Response			
Analysis			
Recommendation 3a	Agree	Estimated Completion Date:	06/30/2024
Please provide details of corrective action or explain disagreement.	DHCD concurs with this recommendation. Reconciliations of loan records are and have been prepared by the loan analyst and reported monthly to the Controller of Loan Accounting. These reconciliations are acknowledged by the Controller’s initials. Management has enhanced the internal controls surrounding this process and those reconciliations are now also subsequently reviewed and acknowledged by the Director of Finance and Accounting. Monitoring dashboards which include aging reports will be available to senior management for review monthly by December 31, 2024. These aging reports will include an action plan for resolving or mitigating any items that have been outstanding for a period of time in excess of 90 days and the plans will be approved by senior management.		
Recommendation 3b	Agree	Estimated Completion Date:	06/30/2025
Please provide details of corrective action or explain disagreement.	DHCD concurs with this recommendation. Although progress had been made in resolving this finding previously, repeated turnover in leadership including the Deputy Director, Director of Loan Accounting and Controller of Loan Accounting levels over the past three years allowed this finding to remain outstanding. In August 2023, the State Funded Loan Program was realigned to report to a different Deputy Director. A new Director of Finance and Administration was hired in January of 2024. A new Controller of Loan Accounting was hired in September 2023 and a new Director of Finance and Accounting was hired in March 2024. Internal controls and monitoring dashboards will be implemented by December 31, 2024, to properly age items for		

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	<p>visibility and monitor the timely resolution of those items for accountability. All analysts are expected to resolve reconciling items within 90 days of identification.</p> <p>To address the existing population of reconciling items, the Department has hired a dedicated analyst to investigate and resolve existing reconciling items. This analyst starts on September 11, 2024. Additionally, existing resources are being deployed to assist with clearing reconciling items. Biweekly meetings with program staff have commenced to obtain missing documentation or address other concerns. Monthly reports to senior and executive management on the progress will be submitted for review and accountability.</p>
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Finding 4

DHCD did not establish policies governing the issuance of Neighborhood Business Works venture debt loans.

We recommend that DHCD establish comprehensive policies governing the issuance of NBW venture debt loans.

Agency Response			
Analysis			
Recommendation 4	Agree	Estimated Completion Date:	10/15/2024
Please provide details of corrective action or explain disagreement.	<p>While DHCD did not publish venture loan underwriting policies, the terms and underwriting procedures were thoroughly reviewed with the internal and external legal counsel for the three NBW Venture loans closed using state appropriated capital. The NBW Venture Debt fundings were part of a “pilot” program during 2019-2021 to develop a new tool to support businesses that could have a strategic economic impact to their communities and the State. During this time, the department put forth legislation, set up a formal credit committee to review and approve venture debt funding, and created the legal documents to support the venture debt transactions.</p> <p>With operational experience gained through the 2019-2021 period, DHCD was able to submit its Venture Debt program as one of eight programs for its State Small Business Credit Initiative (SSBCI) plan to the U.S. Treasury. The Venture Program design and implementation are further detailed in the Department’s SSBCI application. The Venture Debt program was approved by the U.S. Treasury and was awarded up to \$17,000,0000.</p> <p>The department will generate written policies and guidelines for the Venture Debt program by October 15th, 2024.</p>		

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Procurements and Disbursements

Finding 5
DHCD did not comply with State procurement regulations when obtaining marketing services from two vendors and did not monitor services provided by a third vendor to ensure the marketing services were received and amounts invoiced were proper.

We recommend that DHCD ensure marketing contracts are procured in accordance with State regulations and are properly monitored. Specifically, we recommend that DHCD

- a. competitively solicit all services over \$15,000,
- b. execute formal written agreements with vendors as required,
- c. obtain required control agency approval for future contracts and retroactive approval for the contracts above, and
- d. ensure services are received and the related billings are adequately supported and in accordance with the contract terms prior to payment.

Agency Response			
Analysis			
Please provide additional comments as deemed necessary.	The two purchases were concerning the agency’s sponsorships. In response to the audit findings and to align with state procurement regulations, DHCD has developed and implemented a comprehensive policy for sponsorships. This new policy ensures that all sponsorship agreements follow state procurement regulations and includes procedures for competitive solicitation, formal written agreements, and necessary approvals, as applicable.		
Recommendation 5a	Agree	Estimated Completion Date:	Completed
Please provide details of corrective action or explain disagreement.	In response to the audit findings and to align with state procurement regulations, DHCD has developed and implemented a comprehensive policy for sponsorships. This new policy ensures that all sponsorship agreements follow state procurement regulations and includes procedures for competitive solicitation, formal written agreements, and necessary approvals, as applicable.		
Recommendation 5b	Agree	Estimated Completion Date:	Completed
Please provide details of corrective action or explain disagreement.	In response to the audit findings and to align with state procurement regulations, DHCD has developed and implemented a comprehensive policy for sponsorships. This new policy ensures that all sponsorship agreements follow state procurement regulations and includes		

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	procedures for competitive solicitation, formal written agreements, and necessary approvals, as applicable.		
Recommendation 5c	Agree	Estimated Completion Date:	Completed
Please provide details of corrective action or explain disagreement.	In response to the audit findings and to align with state procurement regulations, DHCD has developed and implemented a comprehensive policy for sponsorships. This new policy ensures that all sponsorship agreements follow state procurement regulations and includes procedures for competitive solicitation, formal written agreements, and necessary approvals, as applicable.		
Recommendation 5d	Agree	Estimated Completion Date:	Completed
Please provide details of corrective action or explain disagreement.	The marketing services contract raised in the audit was tied to a marketing vendor who completed work buying media placements for the agency pertaining to a National Homeownership Month campaign. The audit finding claimed there was a lack of documentation to verify if amounts invoiced were proper or if the marketing services paid for were received. The agency received final reports from the vendor displaying that the work placing the Department's advertising was completed and outlining the results of the data tracking for the media placements the vendor made. In addition, the agency viewed physical advertisements (on bus transit) to support its advertising campaign.		

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Information Systems Security and Control

The Office of Legislative Audits (OLA) has determined that the Information Systems Security and Control section, including Findings 6 through 8 related to “cybersecurity,” as defined by the State Finance and Procurement Article, Section 3.5-301(b) of the Annotated Code of Maryland, and therefore is subject to redaction from the publicly available audit report in accordance with the State Government Article 2-1224(i). Although the specifics of the following findings, including the analysis, related recommendations, along with DHCD’s responses, have been redacted from this report copy, DHCD’s responses indicated agreement with the findings and related recommendations.

Finding 6
Redacted cybersecurity-related finding.

Agency Response has been redacted by OLA.

Finding 7
Redacted cybersecurity-related finding.

Agency Response has been redacted by OLA.

Finding 8
Redacted cybersecurity-related finding.

Agency Response has been redacted by OLA.

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