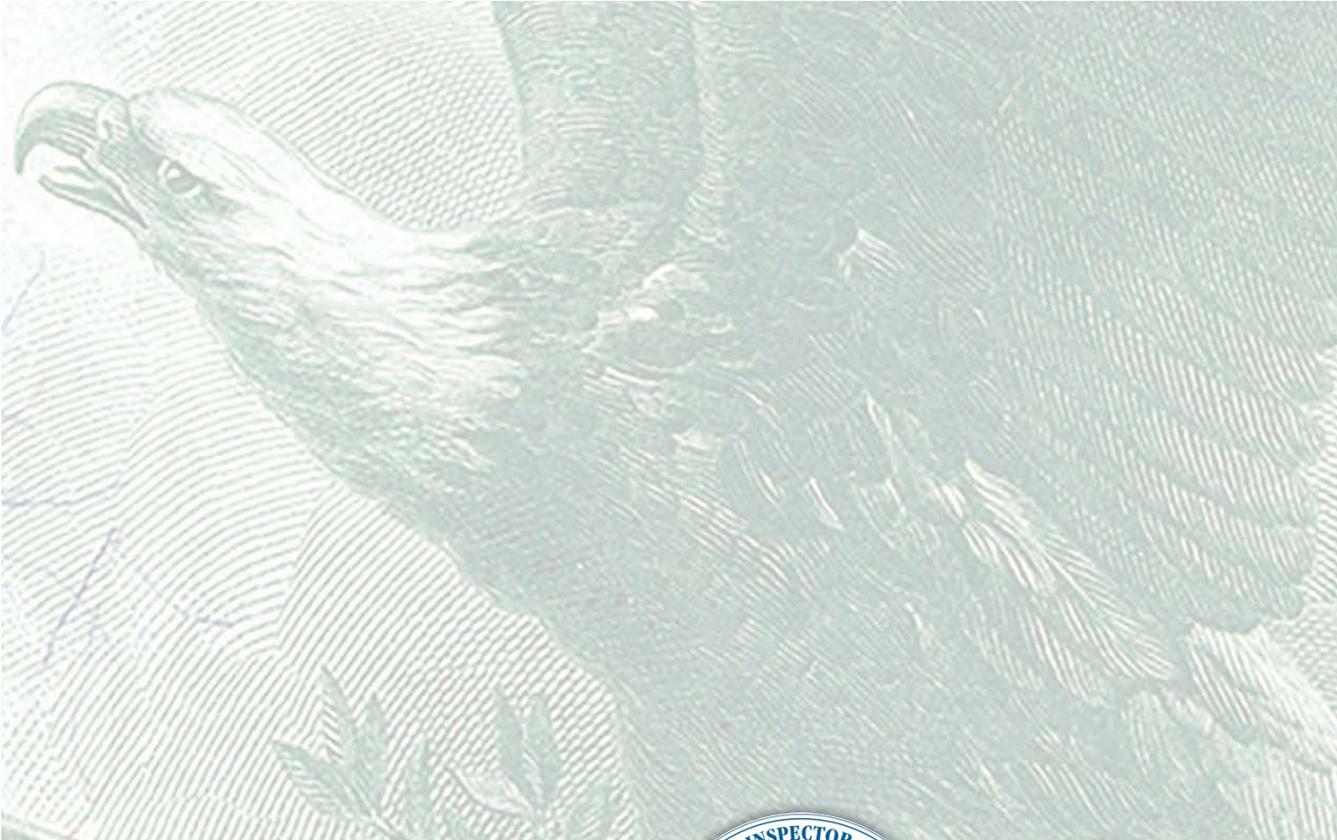




Treasury's HHF Blight Elimination Program Lacks Important Federal Protections Against Fraud, Waste, and Abuse



SIGTARP



OFFICE OF THE SPECIAL
INSPECTOR GENERAL FOR
THE TROUBLED ASSET
RELIEF PROGRAM



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June 16, 2016

MEMORANDUM FOR: The Honorable Jacob J. Lew – Secretary of the Treasury

FROM: **/Signed/**
Honorable Christy Goldsmith Romero – Special Inspector
General for the Troubled Asset Relief Program

SUBJECT: Treasury’s HHF Blight Elimination Program Lacks
Important Federal Protections Against Fraud, Waste, and
Abuse (SIGTARP 16-003)

We are providing this report for your information and use. It discusses risk factors that could impact the effectiveness of the Hardest Hit Fund (“HHF”) Blight Elimination Program.

The Office of the Special Inspector General for the Troubled Asset Relief Program conducted this audit (engagement code 032) under the authority of the Emergency Economic Stabilization Act of 2008 and Public Law 110-343, as amended, which also incorporates the duties and responsibilities of inspectors general under the Inspector General Act of 1978, as amended.

We considered comments from the Department of the Treasury when preparing the report. Treasury’s comments are addressed in the report, where applicable, and a copy of Treasury’s response is included in its entirety.

We appreciate the courtesies extended to our staff. For additional information on this report, please contact Ms. Jenniffer F. Wilson, Deputy Special Inspector General for Audit and Evaluation (Jenniffer.Wilson@treasury.gov /202-622-4633); or Mr. Chris Bosland, Assistant Deputy Special Inspector General for Audit and Evaluation (Christopher.Bosland@treasury.gov /202-927-9321).



Summary

Since 2010, the Troubled Asset Relief Program's ("TARP") Housing Finance Agency Innovation Fund for the Hardest Hit Housing Markets ("Hardest Hit Fund" or "HHF") has provided funds through housing finance agencies in 18 states and the District of Columbia ("HFAs" or the "state HFAs") to homeowners in states hit hardest by the housing bubble. The Hardest Hit Fund has largely been a program to provide Federal funds to unemployed and underemployed homeowners to help pay their mortgage.

Starting in mid-2013, Treasury began allowing seven state HFAs to use existing HHF dollars to demolish vacant and abandoned homes to help neighboring homeowners under a new Blight Elimination Program. At that time, the Department of Housing and Urban Development's ("HUD") Neighborhood Stabilization Program ("NSP") provided \$300 million for blight elimination.

Treasury's Blight Elimination Program allocates nearly \$622 million among seven state agencies, who work with local partners to use contractors and subcontractors to perform the demolition and other work. These local partners pay the contractors or subcontractors and seek reimbursement from the housing agencies for the work performed. The Office of the Special Inspector General for the Troubled Asset Relief Program performed a review of risks that could impact the effectiveness of this program. This work led to a December 14, 2015 SIGTARP Alert Letter to Treasury Secretary Lew advising him that in Evansville, Indiana, this program was being abused to demolish lived-in (rather than abandoned) homes, resulting in people having to leave their homes, so that a car dealership could be relocated.

What SIGTARP Found

SIGTARP found that Treasury's HHF Blight Elimination Program is significantly vulnerable to the substantial risks of unfair competitive practices and overcharging than HUD's program. These risks could lead to fraud, waste, and abuse.

While two Federal programs fund similar activities and entail similar risks, only HUD's program has Federal requirements to protect the Government against substantial risks inherent in contracting for demolition work—Treasury's Hardest Hit Fund does not. As a result, substantial risks under HHF blight elimination continue unchecked for a program that, at nearly \$622 million, is double the size of HUD's program.

SIGTARP found that Treasury's blight elimination program is vulnerable to the risk of unfair competitive practices such as bid rigging, contract steering, and other closed-door contracting processes. SIGTARP found that when Treasury repurposed the Hardest Hit Fund to include blight elimination, it failed to create Federal requirements for full and open competition (and other competition requirements). HUD has a requirement for full and open competition and six pages of other competition requirements in its blight elimination program.

SIGTARP found that Treasury does not require full and open competition for blight elimination contracts. The nearly 280 local partners that award the work include nearly 100 that are individuals, 8 are for-profit companies, 105 non-profit entities, and 33 land banks. These demolition contracts are not subject to any Federal requirement for competitive solicitation or competitive awarding of federal funds, putting the program at significant risk of unfair competitive practices.

Federal requirements for competition are critically important to keep programs fair, drive down costs, motivate better contractor



performance, and help curb fraud, waste, abuse, favoritism, undue influence, contract steering, bid rigging, and other closed-door contract processes. The sole other Federal blight elimination program through HUD has these Federal competition requirements, while preserving flexibility for states.

SIGTARP found that without Federal requirements, most state agencies in HHF do not have their own competition requirements. Only HHF South Carolina has a requirement for full and open competition, which is just 6 percent of the program. State and city competition rules that Treasury relies on exclusively may not even apply because 87 percent of the partners are not municipalities or public agencies. Even when applicable, local rules may be inconsistent.

SIGTARP also found that Treasury's blight elimination program is vulnerable to the risk of overcharging and fraud because, unlike HUD, Treasury has no requirement that Federal funds will only cover blight elimination costs that are necessary and reasonable. Instead, Treasury set a worst-case scenario maximum allowable cost of \$25,000 or \$35,000 per property depending on the state. Treasury has no way of knowing whether the demolition and other costs submitted for Hardest Hit Fund dollars are necessary and reasonable, and is at a significant disadvantage in identifying waste, fraud and abuse.

Treasury's Blight Elimination Program leaves decisions about what costs are necessary and reasonable, and about whether and in what form to have competition in the solicitation and award of contracts, to the recipients of Federal funds. HUD does not place such trust or hope in recipients to protect the Federal government.

The requirements of a grant program (at HUD) should be the bare minimum for a TARP program. HHF does not have to be a grant for Treasury to protect it. That would

be form over substance. Federal grant funds are not the only Federal funds that should be protected. It is a long-standing practice for the Federal Government to establish requirements to protect Federal programs when it provides substantial funding. The other large TARP housing program HAMP has a comprehensive set of Treasury requirements to protect the program and the Government.

Treasury should take action now by creating Federal requirements similar to those HUD imposes in its blight elimination program to require full and open competition and limit costs to only those that are necessary and reasonable. Treasury recently expanded this program allocating more than \$100 million. There are hundreds of millions of dollars (\$458 million) left to be spent in this program, and three out of seven states have not reported any demolitions.

There is no harm in Treasury creating Federal requirements for full and open competition, and other competition requirements, similar to those HUD imposes. HUD allows for the same locally-tailored solutions and flexibility that Treasury seeks. The Hardest Hit Fund should be inflexible to fraud, waste, and abuse.

What SIGTARP Recommends

Treasury could have used HUD as a model or adopted its own requirements to mitigate the inherent risks of unfair competition and overcharging, and they can still do so now by following SIGTARP's 20 recommendations made in this report. In essence, SIGTARP recommends that Treasury's program have the same protection as HUD's blight elimination program for competition, and the same limit on only covering those costs that are necessary and reasonable.

In commenting on a draft of this report, Treasury stated that it will look at SIGTARP's recommendation at a later date.



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Introduction and Background

Treasury's Housing Finance Agency Innovation Fund for the Hardest Hit Housing Markets ("HHF") program, launched in 2010, provided Federal dollars to "help families in the states that have been hit the hardest by the aftermath of the housing bubble." According to Treasury, as of December 31, 2015, most (75%) of those funds were used by 19 housing finance agencies ("HFAs" or the "state HFAs") to help unemployed or underemployed homeowners pay their mortgage.¹ Treasury entered into HHF agreements with these state HFAs to flow the money through them to homeowners. The agreements are the sole governing document for each state HFA's Hardest Hit Fund programs, as Treasury has no Federal rules for HHF outside of these agreements.

HHF has struggled to reach homeowners. This is particularly true in certain states where low percentages of homeowners who apply actually receive help. As SIGTARP reported in April 2012, HHF had spent only \$217.4 million to help 30,640 homeowners—approximately 3% of the TARP funds allocated and approximately 7% of the number of homeowners estimated to be helped in the program.²

At that time, the U.S. Department of Housing and Urban Development ("HUD") had a program to demolish vacant and abandoned houses that bring down property values. HUD committed approximately \$300 million to the clearance of blighted properties under the Neighborhood Stabilization Program ("NSP") in the form of Federal grants.³ HUD adopted its own requirements that apply to the recipients of the Federal funds it disburses for demolition. Even though HUD left flexibility with the recipients who make contracting decisions (states, local governments, and non-profit entities), it required those entities to adhere to Federal requirements.⁴ The HUD NSP program has expended its Federal funds for blight elimination.

¹ The 19 participating HHF jurisdictions are: Alabama, Arizona, California, Florida, Georgia, Illinois, Indiana, Kentucky, Michigan, Mississippi, Nevada, New Jersey, North Carolina, Ohio, Oregon, Rhode Island, South Carolina, Tennessee, and Washington, D.C.

² See SIGTARP, "Factors Affecting Implementation of the Hardest Hit Fund Program," April 12, 2012.

³ HUD's NSP was first authorized by the Housing and Economic Recovery Act of 2008 and, later, the American Recovery and Reinstatement Act of 2009 and the Dodd-Frank Financial Reform and Consumer Protection Act of 2010. HUD distributed the funds to state and local governments who were allowed to use NSP funds for a number of eligible activities, including rehabilitating abandoned or foreclosed properties, establishing land banks, demolishing blighted structures, and redeveloping vacant or demolished properties.

⁴ 2 C.F.R. §§ 200.317-326 (effective December 26, 2014). Prior to December 26, 2014, Federal awards made under HUD's NSP demolition grant program were governed by the regulations in effect and codified in 24 C.F.R. Part 84 (pertaining to non-profit organizations) and 24 C.F.R. Part 85 (pertaining to state and local governments). The procurement-related requirements in the pre-2015 HUD regulations were substantially



In mid-2013, Treasury followed HUD's lead and approved HHF funds for the demolition and greening of vacant and abandoned blighted properties. Treasury's purpose with this program is to prevent foreclosures of neighboring homeowners. Before approving this new use of TARP funds, Treasury conducted a written analysis of the benefits of blight elimination. This Treasury document (or any Treasury document provided to SIGTARP) fails to show a Treasury analysis of the risks associated with blight elimination.

This month, Treasury allocated more than \$100 million in additional Federal funding for blight elimination. The HHF Blight Elimination Program is more than double the size of blight elimination under HUD's NSP program. Treasury had allowed 7 of 19 state HFAs to reallocate nearly \$622 million from homeowner programs to demolition programs as of June 1, 2016, as set forth in Table 1. These are not Federal grants.

TABLE 1: TARP Blight Elimination Program HHF Allocations and Demolitions as of June 1, 2016

State HFA	Total HHF Allocation*	Funds Available For Blight Elimination	Number of Homes Reported Demolished As of 3/31/ 2016
Alabama	\$162,521,345	\$25,000,000	0
Illinois	\$715,077,617	\$20,509,804	0
Indiana	\$283,714,437	\$75,000,000	590
Michigan	\$761,204,045	\$381,185,566	8,531
Ohio	\$762,302,067	\$79,489,572	2,009
South Carolina	\$317,461,821	\$35,000,000	26
Tennessee	\$302,055,030	\$5,500,000	0
Totals	\$3,304,336,362	\$621,684,942	11,156

* Treasury had announced on April 20, 2016 additional funding for certain states under the fifth round of HHF funding, but had not yet formalized all of those allocations, including those specific to the HHF Blight Elimination Program, with the applicable state housing finance agencies.

Sources: Treasury; HFA Participation Agreement Schedule B, Service Schedules, and Quarterly Performance Reports for respective states.

Treasury's repurposing of HHF opened the door to significant Federal TARP payments being made to an entirely different set of recipients than the struggling homeowners who the program was originally intended to benefit. TARP funds originally earmarked for homeowners now flow to demolition and other contractors and subcontractors engaged by intermediary local partners responsible for carrying out program activities. These program activities include pre-and post-demolition activities such as asbestos surveys, asbestos remediation, geo-

similar to those subsequently incorporated into 2 C.F.R. Part 200. For simplicity, this report only cites HUD's more recent requirements under 2 C.F.R. Part 200.



engineering surveys, environmental studies, removal of trash and debris, grading of land, greening of land, and maintenance.

Most (87%) of the nearly 280 local partners in the HHF Blight Elimination Program are not municipalities or public agencies. For example, there are nearly 100 individuals and 8 for-profit companies who serve as local partners. There are 105 non-profit entities and 33 land banks. The local partners generally use and pay contractors (and subcontractors) to perform the demolition and other services (although some may also perform the work themselves), and seek reimbursement from TARP funds.

We initiated this audit as part of our continuing oversight of TARP. The specific objective of this audit was to consider risk factors that could impact the effectiveness of the HHF Blight Elimination Program. SIGTARP conducted this audit in accordance with generally accepted government auditing standards established by the U.S. Government Accountability Office. For a complete discussion of the audit scope and methodology, see Appendix A.

This report highlights the key risks to taxpayers caused by the lack of Federal protections built into the HHF's Blight Elimination Program, particularly when compared to the protections that exist under the similar demolition program overseen by HUD.



Treasury Repurposed the Hardest Hit Fund to Include Blight Elimination Without Repurposing Its Oversight

Helping homeowners by providing Federal funds to pay their mortgages and avoid foreclosure is a completely different purpose than doling out Federal funds through contracts to non-Federal entities and individuals to demolish abandoned houses. This new purpose was unlike anything Treasury had ever done with TARP or elsewhere.

Blight elimination and demolition were new to Treasury, entailing new activities, new types of participants, and new risks to the Government. Unlike the homeowner-recipient HHF programs, the Hardest Hit Fund's repurposing allowed Federal funds to flow through a series of contracts to nearly 280 local partners (including individuals). These local partners are responsible for the demolition, greening, and subsequent maintenance of vacant and abandoned properties, including contracting with demolition and other contractors and subcontractors.

Repurposed programs require repurposed oversight, but that did not happen. Such a substantial change required Treasury to conduct a complete assessment of the risks attendant to this flow of what would later become more than half a billion Federal dollars to non-Federal recipients. Treasury never made that assessment. Such a substantial change should require a new approach to oversight to protect the Federal Government and this program. At the start, Treasury should have implemented a comprehensive set of requirements to protect the program from fraud, waste, and abuse, which Treasury could then later ensure were followed. This did not happen.

The vulnerability of the Hardest Hit Fund to fraud, waste, and abuse significantly increased with blight elimination, which Treasury could have mitigated, but did not. With nearly 280 local partners—the identities of which are not required to be reported to Treasury—receiving Federal funds, entering into a multitude of contracts, and responsible for carrying out the activities under the program, the risks are substantial.

Protecting the program and mitigating risks of fraud, waste, and abuse with a comprehensive set of Treasury requirements would not have been too difficult or time consuming, because HUD had a similar program with comprehensive Federal requirements to mitigate vulnerabilities to fraud, waste, and abuse. HUD's requirements are in 6 small-font pages of



Federal regulations related to grants and cooperative awards. Treasury did not apply these regulations to HHF because HHF is not a grant, but rather a purchase of a financial instrument.

A Federal program does not have to be in the form of a grant to have comprehensive Federal requirements. It is a long-standing practice for the Federal Government to establish requirements to protect Federal programs when it provides substantial funding. One example is the other TARP housing program, the Home Affordable Modification Program (“HAMP”), which has a comprehensive set of Treasury requirements to protect the program and the Government. The fact that Treasury desires state flexibility for HHF does not eliminate the need for a comprehensive set of Federal requirements, because HUD gives municipalities’ similar flexibility in its blight elimination program. Flexibility does not mean free reign. HUD allows for flexibility under a set of Federal requirements.

Even though Treasury had no experience with blight elimination, unlike HUD, Treasury did not implement a comprehensive set of requirements that would protect the Government—even though the same risks are inherent in both Treasury’s and HUD’s blight elimination programs. Rather than revise its agreements with state agencies to implement requirements addressing all of the risks associated with blight elimination, Treasury only added to those agreements a two- to three-page service schedule typed in large font that simply summarizes at a high level how the blight program will work in each state.

Treasury’s existing agreements with state agencies are not sufficient to protect this program against fraud, waste, and abuse because they were designed for homeowner-focused HHF programs. The existing agreements never addressed the types of activities related to demolition or the risks involved. The applicable laws listed in the agreement are largely homeowner protection laws. That made sense when the program was only homeowner-focused. When it repurposed HHF to encompass blight elimination, Treasury neither enacted its own set of protections for demolition-related activity nor mimicked HUD’s protections. At least one city mayor has said that these Federal funds come with no stipulations. As the steward of more than half a billion taxpayer dollars, Treasury has the ultimate oversight responsibility to ensure that TARP programs are effective, and to protect TARP dollars and programs from fraud, waste, and abuse. It is not too late to do so, given the new Federal dollars Treasury recently awarded under HHF.



In Stark Contrast with HUD, Treasury Does Not Limit Federal Dollars to Only Those Costs That Are Necessary and Reasonable for Blight Elimination Activities, Leaving the Federal Government at Risk of Overpaying, Waste, and Fraud

SIGTARP found that Treasury has no requirement that Federal funds will only cover costs related to blight elimination activities that are necessary and reasonable, leaving the Federal Government at risk compared to HUD's blight elimination program. When recipients of HHF program funds were homeowners at risk of foreclosure—those intended to benefit from the program—there may have been less of a need for Treasury to ensure that Federal dollars only covered program costs that were necessary and reasonable. That changed in mid-2013 when Treasury decided that these Federal dollars would also go through state agencies to local partners to pay contracts for the demolition of vacant and abandoned houses. Unlike HUD's demolition program, for which the vast majority of recipients are states and local governments, only 13% of the local partners in Treasury's program are municipalities or public agencies. Of the local partners, nearly 100 are individuals and 8 are for-profit companies.

Treasury's Agreements with State Agencies Do Not Limit Federal Dollars Only to Necessary and Reasonable Demolition Costs

SIGTARP found that despite Treasury substantively changing the nature of the Hardest Hit Fund to a program that doles out significant Federal funding through contracts to non-Federal entities or individuals, and their contractors or subcontractors, Treasury did not substantively change its requirements for limiting program costs in its participation agreements with state agencies. As a result, the nearly \$622 million available for local partners (and any of their contractors or subcontractors) in Treasury's program is not subject to any Federal requirement that costs submitted must be necessary and reasonable, putting the Federal Government at risk of overpaying, waste, and fraud.

Both HUD and Treasury place the day-to-day decision-making and administration of their respective blight elimination programs in the hands of local entities (states, local governments, and non-profits for HUD; state housing finance agencies and their local partners for Treasury). However, unlike Treasury, HUD's requirement that costs be



necessary and reasonable governs the day-to-day decisions made by local entities when expending Federal funds.

One of the largest blight elimination programs that many cities in these states participate in, other than HHF, is HUD's Neighborhood Stabilization Program ("NSP") under the Community Development Block Grant program ("CDBG"). HUD's NSP grant program has Federal requirements that allowable costs must be necessary and reasonable for performance.⁵

HUD's program is not the only blight elimination program that requires that performance costs be necessary and reasonable to be paid. State-funded demolition under the Michigan Blight Elimination Program funded by an Attorney General settlement also limits allowable cost to "Only reasonable and necessary costs that are directly related to demolition...."⁶

Unlike HUD, Which Has Established a Federal Requirement to Limit Paying for Blight Elimination Costs That Are Not Necessary and Reasonable, Treasury Allows for Unnecessary and Unreasonable Costs as Long as They Fall Under a Maximum Set Amount That Is Based on Worst-Case Scenario of Costs

In what appears to be a holdover from previous versions of Treasury's agreements with state agencies that limit Federal dollars for assistance (unemployment or other assistance) to a maximum allowable cost per homeowner, Treasury has set a maximum allowable cost per property for blight elimination activities. While this may have been sufficient to protect taxpayers against risks when the HHF recipients were those that Treasury intended HHF to help—homeowners—these terms are not sufficient to protect taxpayers adequately when the recipients of Federal dollars are not homeowners. Treasury did not intend to use HHF to bail out the recipients of Federal dollars for blight elimination activities. Most

⁵ See 2 C.F.R. §200.403 (a). A "Federal award" is defined as Federal financial assistance that a non-Federal entity receives directly from a Federal awarding agency or indirectly from a pass-through entity. See 24 C.F.R. §570.502 Recipients of CDBG funds shall comply with 24 C.F.R. Part 85 incorporating the OMB's Cost Principles at 2 C.F.R. Part 200. Treasury takes the position that HHF is not a grant program. OMB's cost principles also apply beyond grants to cooperative agreements, which differ from grants because of the substantial involvement of the Federal agency. See 2 C.F.R. §200.24.

⁶ See 2015 Michigan Blight Elimination Program Statement and Application Program Statement, https://www.michigan.gov/documents/landbank/Blight_Elimination_2015_Application_rev054205_488600_7.pdf, accessed 12/16/2015. The Moving Ohio Forward program (now discontinued), which was funded by an Attorney General settlement and used as a model for the HHF program, had a goal "to maximize the number of demolitions of blighted, vacant or abandoned residential structures." See Moving Ohio Forward Grant Program Demolition Guidelines, May 4, 2012 (Revised June 21, 2012), <http://www.ohioattorneygeneral.gov/OhioAttorneyGeneral/files/f4/f4882fe3-4cac-40c4-8a29-a2f45a8bf157.pdf>, accessed 12/16/2015.



(87%) of these recipients are not cities or public agencies, but are instead individuals, for-profit entities, non-profit entities, or land banks, who may be contracting the work out to demolition contractors and their subcontractors. In approving blight elimination as a permissible use of TARP, Treasury changed who will receive TARP funds, but did not change its program requirements to protect against this new risk of overpaying, waste, and fraud.⁷

Treasury's maximum allowable cost per property (of \$25,000 or \$35,000) is not sufficient to protect against overpaying, waste, and fraud, because it does not reflect necessary and reasonable costs, but instead far exceeds the average cost of demolition to account for a worst-case scenario.⁸ The median cost of demolition under HHF reported to Treasury as of December 31, 2015, is \$10,558 (with an additional median greening cost of \$2,700) in Michigan HHF, \$14,918 (with an additional median acquisition cost of \$5,021 and an additional median greening cost of \$4,441) in Indiana HHF, and \$8,100 (with an additional median acquisition cost of \$108 and an additional median greening cost of \$500) in Ohio HHF. Treasury has no way of knowing whether even these median numbers reflect necessary and reasonable costs. According to an official from Ohio's HFA, the \$25,000 limit allows partners to deal with "hot houses," those with a lot of asbestos. Setting limits on cost aimed at the worst-case scenario does not protect a program from overpaying, waste, and fraud.

With no Treasury requirement to limit Federal dollars to only those demolition costs that are necessary and reasonable, Treasury is not conducting any oversight to ensure that Federal funds do not go to unnecessary or unreasonable costs. Treasury conducts oversight through on-site compliance reviews. However, Treasury's compliance staff is looking to determine whether Treasury's requirements are followed, and here there is no Treasury requirement that program costs be necessary and reasonable.

⁷ In addition, Treasury only requires extremely limited reporting by state HFAs on costs. Treasury requires no reporting of costs at a city level, only at a state level. Even at a state level, Treasury only requires state HFAs to report median costs, rather than the range of actual costs. Treasury also only requires reporting on three composite activities (acquisition, demolition, and greening), which each comprise multiple subcomponents, particularly demolition. In its April 2015 audit report, "Treasury Should Do Much More to Increase the Effectiveness of the TARP Hardest Hit Fund Blight Elimination Program," SIGTARP recommended that Treasury collect and report detailed cost information at the local partner contractor and subcontractor level. Treasury has not implemented that recommendation, limiting the insight of Treasury, SIGTARP, and taxpayers who fund this effort, and limiting the ability to conduct oversight.

⁸ Treasury's agreement with Illinois and South Carolina provide maximum allowable costs of \$35,000 per property, while its agreement with Alabama, Indiana, Michigan, Ohio and Tennessee provide a maximum of \$25,000 per property.



Treasury Appears to Be Relying on State Agencies to Limit Costs, but Those Agencies Do Not Limit Federal Funds to Only Costs That Are Necessary and Reasonable, and Instead Rely Heavily on the Judgment of Those Receiving the Federal Funds

In stark contrast with HUD, Treasury has no requirement that this program does not pay more than it has to for demolition costs. Every TARP dollar wasted in demolishing one property is one less dollar available to fund impactful demolition of other abandoned “zombie” homes in that city. A Treasury internal action memo approving the creation of the Blight Elimination Program for HHF states, “Further economies of scale savings will be investigated to drive costs down throughout all communities served for the [Blight Elimination] program.” However, Treasury made no requirement to drive down costs. With no Treasury requirement, the state housing finance agencies may not understand that they have a duty to minimize costs.

None of the state agencies in Treasury’s program have a requirement that Federal dollars will only cover demolition costs that are necessary and reasonable. Officials from state agencies told SIGTARP that Treasury did not give them guidance on cost other than the maximum amount per property.

Without a Federal requirement, Treasury’s HHF Blight Elimination Program leaves the analysis on what demolition costs are necessary and reasonable to the recipients of Federal funds.

An official from Michigan’s HFA told SIGTARP that the costs are “pretty much left up to the blight partner. Also, with their goal in mind to take down as many properties, they’re going to be prudent about their costs.”

Two officials from Indiana’s HFA told SIGTARP that awarding each city a set dollar amount gives incentive to keep costs down, with one official telling SIGTARP that this incentive is the guard against waste and abuse.

Three state housing finance agencies (Ohio, Michigan, and Indiana) that have already used TARP to reimburse demolitions currently review costs only after invoices come in. SIGTARP also found that supporting documentation was lacking in some instances. These state agencies do not ensure those costs are necessary and reasonable, and rely on the local partners to minimize costs.

A Federal program that is more than half a billion dollars requires more than trust or a hope that costs will be minimized. There must be Federal



requirements in place to ensure that happens. HUD has those requirements. Treasury does not.

At the very least, Treasury's program should have the same protection as the other Federally-funded blight elimination program run by HUD to ensure that Federal dollars are only used for necessary and reasonable demolition costs of demolition. The requirements of grant programs should be the bare minimum of what Treasury requires in TARP, given the extraordinary nature of the TARP bailout.

Treasury Should Require State Agencies to Do More to Establish in Writing What Are Necessary and Reasonable Demolition Costs in Each City and Seek Substantial Justification for Invoices That Exceed Those Costs

Treasury should require that state housing finance agencies do more to establish in writing necessary and reasonable demolition costs for each city. Armed with written analysis about the necessary and reasonable costs, the state HFAs should seek and analyze justification for invoices that exceed those costs. Properties that are to be demolished may vary, with some demolitions being straightforward and others posing greater challenges such as "hot houses" with high levels of asbestos. These variances illustrate the need for the state agencies to establish for each city: (1) the necessary and reasonable cost of demolishing a standard house; as well as (2) the necessary and reasonable cost of removing a lot of asbestos in a "hot house." This information is the due diligence necessary for effective review of claims for Federal funds. If the claims exceed the established necessary and reasonable costs for demolishing a standard house, the state agencies should engage in higher scrutiny requiring substantial justification.

To arm them with knowledge, state agencies should at a minimum follow the best practices of HUD and other Federal awards. For example, Federal law provides that for Federal awards, a cost is reasonable if it does not exceed that which would be incurred by a prudent person under the circumstances, giving consideration to such things as:

- Whether the cost is a type generally recognized as ordinary and necessary,
- Restraints that come from factors such as sound business practices and arms-length bargaining,
- Market prices for comparable services for the geographic area,



- Whether the individuals acted with prudence, and
- Whether the non-Federal entity significantly deviates from its established practices and policies regarding the incurrence of costs.⁹

The state agencies are not doing enough now to ensure that demolition costs are minimized. While the head of Indiana's HFA told SIGTARP, "it would be fairly easy to recognize from our perspective if the cost associated particularly with demolition in Indianapolis—which is one of the places that does ongoing demolition—it would be very easy to recognize whether or not those costs were inflated versus what the standard market rates are going to be." However, it is unclear what the state agency is using as a standard market rate, or how that would be translated to HFA staff reviewing claims. Further, this type of "know-it-when-you-see-it" review process makes oversight difficult, if not impossible.

A reactive approach in establishing what costs are necessary and reasonable by reviewing submitted claims carries a risk that those who are submitting invoices could drive up the price. Without a written analysis of necessary and reasonable costs, it is very difficult for staff to review claims in a consistent manner ensuring that Federal funds do not pay for unnecessary or unreasonable demolition costs. The Director of Operations for Indiana's HFA described its claims review process as making sure that the appropriate documents are provided and that the invoices match up with the amounts claimed. Even with that limited review process, he told SIGTARP that claims review has been a challenge because it is unlike any of the other programs they review, which puts stress on the claims review staff.

Treasury should require that state agencies participating in blight elimination under HHF determine the reasonable and necessary costs for each city using all three best practices:

1. **Using independent industry experts to develop necessary and reasonable costs:** Whether or not the state agency has experience administering a blight elimination program, turning to an independent expert working on behalf of the TARP program, rather than another program, can help protect against TARP overpaying. This requirement would be in keeping with HUD's NSP program that follows cost guidelines to ensure that project costs are reasonable by conducting cost analysis using appropriate

⁹ 2 C.F.R. § 200.404.



cost estimating manuals or services.¹⁰ Some cities in HHF may be following NSP's guidelines because they are also HUD grantees, and some cities may not be for this program because there is no requirement to do so. However, state agencies cannot conduct adequate oversight over that if they have not independently determined necessary and reasonable costs. In addition, not all HHF local partners are cities that follow NSP guidelines. Only 13% of the local partners are municipalities or public agencies. With nearly 100 individual local partners, and land banks, non-profit organizations, and for-profit organizations, state agencies should not be relying on local partners to know and keep to only those costs that are necessary and reasonable. An independent determination of costs is an industry best practice that Treasury and the entities it contracts with—state agencies—could use to establish an objective standard demolition baseline for determining the reasonableness of a contractor/subcontractor's invoice. This independent expert could review historical costs, and current costs in the market for this work. An independent expert can help state agencies conduct the due diligence they need to determine the reasonable and necessary cost of performance to achieve a more comprehensive and accurate estimate of the expected costs. The independent expert can also help state agencies determine what is a reasonable and necessary cost when problems arise such as environmental issues or asbestos.

2. **Third-party fair market price quotes in each city:** HUD's NSP program follows cost guidance under CDBG, which provides guidelines that seek to ensure that project costs are reasonable by obtaining third-party *fair market* price quotes. This guidance provides that any recipient should pay particular attention to any cost element of the project that will be carried out through a non-arms-length transaction.¹¹ For HUD NSP, it is the city that would obtain these quotes because the city is HUD's grantee. In Treasury's HHF, however, the state agency receives the Federal funds, but does not obtain the market quotes, instead relying on the local partner.
3. **Established practices and policies regarding the incurrence of current and historical costs:** Obtaining current and historical cost information on Federal, state and local blight elimination, particularly by the same parties conducting demolition in HHF, is a necessary part of a state agency's due diligence to determine

¹⁰ See 24 C.F.R. § 570, Appendix A.

¹¹ See 24 C.F.R. § 570, Appendix A.



necessary and reasonable costs. The cost of demolition under HHF has risen from prior non-HHF demolitions in some of these states. For example, the Moving Ohio Forward program used \$75 million in proceeds from an Attorney General lawsuit against mortgage servicers to demolish vacant, blighted, or abandoned structures. Under this program, the Ohio Attorney General's Office razed 14,608 structures between February 2012 and December 2014, at an average total blight elimination cost of about \$8,150. That is nearly \$4,000 less than the average total blight elimination cost reported under Ohio's version of the HHF Blight Elimination Program as of December 31, 2015.¹²

Similarly, the State of Michigan's (non-HHF) Blight Elimination Program allocated \$10 million from the Attorneys-General settlement to the City of Detroit to eliminate blight near select "Pathways to Potential" schools. Under that program, the Michigan Land Bank (which is also a program partner under HHF) completed 768 demolitions as of August 15, 2014 (the most recent report available on the Land Bank's website) at an average total blight elimination cost of approximately \$10,400 per property¹³—compared to almost \$15,000 in total blight elimination costs per property reported by Michigan's HFA under HHF through December 31, 2015. However, the state agencies are not armed with the knowledge to understand and question those costs. State agencies should require that each local partner provide their established practices and policies regarding the incurrence of historical costs. They should also require submission of practices and policies for exceeding those costs (such as the presence of asbestos and other environmental hazards), and any other reason to deviate from those established practices and policies. Obtaining these established practices and policies would provide the state agencies with information to determine what costs are necessary and reasonable for regular demolitions and what justifications and expenses are necessary when challenges arise that may raise costs, but may still be considered necessary and reasonable.

TARP's housing programs also deserve as much protection as TARP's programs for too big to fail institutions and other banks. Treasury took just such a three-layered approach in TARP investment programs to sell a

¹² Average cost is determined by dividing the total assistance by the number of properties demolished.

¹³ Michigan State Housing Development Authority, "Report of the Michigan Land Bank Fast Track Authority of the State of Michigan," for the period of October 1, 2010, through September 30, 2012 and October 1, 2012 through September 30, 2014, no date, http://www.michigan.gov/documents/landbank/FINAL_DRAFT.ALLDOCS.v6.093014_491480_7.pdf, accessed 5/13/2016.



TARP recipient's stock warrants. When exiting TARP, TARP institutions wanted to repurchase their warrants from Treasury. Because warrants of this duration were not typically traded on an exchange, Treasury assessed the TARP recipient's repurchase offer to determine if it reflected fair market value using three different methodologies: (1) market quotes—bids solicited from 10-15 firms; (2) Treasury's financial modeling valuations using two financial models; and (3) Treasury's hired independent industry experts (using 1 to 8 external asset managers hired by Treasury).¹⁴ If Treasury can take a three-layered approach to protect against overpaying for warrants, it should take a similar approach against overpaying for demolition.

Public Policy Interests Support Treasury Protecting This Program to the Same Extent as HUD's Program by Requiring That Costs Be Necessary and Reasonable for the Remaining Hundreds of Millions of Federal Dollars (\$458 Million) Still Available

Treasury can require that blight elimination activity costs be necessary and reasonable to promote the same public policy interests and protect against the same risks that are present in HUD's blight elimination program. Several of the state agencies have not yet reported any demolition activity. Treasury has recently expanded the Hardest Hit Fund program with additional \$2 billion, some of which will go to blight elimination.

There are significant policy reasons for Treasury protecting this program at least to the same extent as HUD. When creating TARP, Congress articulated a public policy interest in minimizing the impact on the national debt and long-term costs. Section 103 of the Emergency Economic Stabilization Act ("EESA"), the law authorizing TARP, provides that when exercising his TARP authority, the Secretary of the Treasury has a duty to protect the interests of taxpayers by minimizing the impact on the national debt.¹⁵ In addition, section 113 of EESA provides that the Secretary will use the TARP authority to minimize any potential long-term costs. Treasury's duty under the TARP law also flows to the state housing finance agencies. Treasury's agreement with state agencies requires state agencies to comply with the TARP law.

¹⁴ See SIGTARP, "Assessing Treasury's Process to Sell Warrants Received from TARP Recipients," May 10, 2010.

¹⁵ See Emergency Economic Stabilization Act Section 103 "Considerations. In exercising the authorities granted in this Act, the Secretary shall take into consideration (1) protecting the interests of taxpayers by maximizing overall returns and minimizing the impact on the national debt."



Treasury recognizes the public interests that Congress required. Treasury's Office of Financial Stability which administers TARP has four operational goals, one of which is to continue helping struggling homeowners avoid foreclosure and another is to fulfill its requirement under EESA to minimize the cost of TARP programs to the taxpayer.¹⁶ According to Treasury's latest financial report, Treasury "...manages TARP investments to minimize costs to taxpayers by managing the timely exit of these investments to reduce taxpayers' exposure," however Treasury did not address how it minimizes the cost of TARP housing programs to the taxpayer.¹⁷

Throughout TARP, Treasury has publicly stated that it conducts risk assessment and takes action to mitigate risk.¹⁸ For Treasury in the last few years, these efforts have focused on determining when to sell its interest in TARP banks to maximize returns to taxpayers and minimize losses. Treasury also has a duty to minimize the cost of TARP's Blight Elimination Program to taxpayers. Treasury should conduct the same risk assessment and take action to mitigate risk that TARP will overpay demolition contractors and subcontractors. Treasury can do this by, at the very minimum, following the best practices and requirements of HUD's blight elimination programs to limit Federal dollars to only those blight elimination costs that are necessary and reasonable. If fewer TARP dollars are spent on individual demolitions, more abandoned "zombie" properties can be demolished, and more neighboring homeowners helped to avoid foreclosure.

Treasury has stated one of its management objectives is to ensure that TARP programs and resources are free from waste, fraud and mismanagement.¹⁹ Spending anything more in TARP funds than is necessary and reasonable amounts to waste, and could open this TARP program up to abuse or fraud.

¹⁶ See Treasury, "Agency Financial Report: Office of Financial Stability – Troubled Asset Relief Program", Fiscal year 2014, <https://www.treasury.gov/initiatives/financial-stability/reports/Documents/FY2014%20OFS%20AFR%20FINAL%20-%20Nov%206%202014.pdf>, accessed 12/10/2015.

¹⁷ See Treasury, "Agency Financial Report: Office of Financial Stability – Troubled Asset Relief Program", Fiscal year 2014, <https://www.treasury.gov/initiatives/financial-stability/reports/Documents/FY2014%20OFS%20AFR%20FINAL%20-%20Nov%206%202014.pdf>, accessed 12/10/2015.

¹⁸ See Treasury, "Agency Financial Report: Office of Financial Stability – Troubled Asset Relief Program", Fiscal year 2014, <https://www.treasury.gov/initiatives/financial-stability/reports/Documents/FY2014%20OFS%20AFR%20FINAL%20-%20Nov%206%202014.pdf>, accessed 12/10/2015.

¹⁹ See Treasury, "Agency Financial Report: Office of Financial Stability – Troubled Asset Relief Program", Fiscal year 2014, <https://www.treasury.gov/initiatives/financial-stability/reports/Documents/FY2014%20OFS%20AFR%20FINAL%20-%20Nov%206%202014.pdf>, accessed 12/10/2015.



Unlike HUD, Which Has Significant Federal Requirements Compelling Competition in Its Blight Elimination Program, Treasury Does Not Require Full and Open Competition (or Any Competition) for Nearly \$622 Million in Federal Funds for Blight Elimination Leaving the Federal Government at Substantial Risk

SIGTARP found that Treasury has no requirement for full and open competition (or any requirements for competition) for its blight elimination program, leaving the Federal Government substantially at risk compared to HUD's blight elimination program. When the Hardest Hit Fund was focused on providing Federal funds to homeowners at risk of foreclosure, there was no need for Treasury to have program requirements to address competition. However, in mid-2013 Treasury changed the program so that state housing finance agencies would send Federal funds through local partners, some who might contract or subcontract the work out. Most (87%) of the local partners are not municipalities or public agencies. For example, there are nearly 100 individuals and 8 for profit-companies who serve as local partners who have received and/or may receive these Federal funds.

Treasury's Agreement with State Agencies Is Silent as to Competition

SIGTARP found that despite Treasury substantively changing the nature of the Hardest Hit Fund from providing direct benefits to homeowners to also doling out significant Federal funding through contracts to non-Federal entities and individuals, Treasury did not substantively change its program requirements to address the need for competition for these Federal funds. As a result, the nearly \$622 million available for local partners (and any of their contractors or subcontractors) in Treasury's program is not subject to a requirement for full and open competition and is not subject to any Federal requirement for competitive solicitation or competitive awarding of Federal funds, putting the Federal Government at substantial risk.

Both HUD and Treasury place the day-to-day decision-making and administration of their respective blight elimination programs in the hands of local governments or government agencies (cities and other local governments for HUD, state housing finance agencies for Treasury).



However, unlike Treasury, HUD sets requirements and rules for competition in its Neighborhood Stabilization Program that govern the day-to-day decisions made by cities and other local governments. HUD does not rely on applicable state or local laws or rules, or rely on the local government receiving the Federal dollars to determine rules on competition.

HUD requires “full and open competition” in its blight elimination program.²⁰ Treasury does not. Under HUD, NSP committed fewer Federal funds for demolition (approximately \$300 million) than Treasury’s program (approximately \$622 million).

Treasury does not need to adopt the same Federal regulations that apply to HUD’s program to protect Treasury’s program. Treasury has taken the position that TARP funds are not grant funds like the HUD funds and, accordingly, the Federal regulations requiring full and open competition and other competition requirements do not apply. That is form over substance. Treasury is not precluded from imposing its own requirements or adopting similar principles. Treasury can and should protect the program by requiring competition.

Treasury Appears, Through Its Silence, to Be Relying on State Agencies or State or Local Laws That May or May Not Apply, Unlike HUD, Which Has Established Federal Rules for Competition and Does Not Rely on Local Governments or State/Local Laws/Rules That May Apply

Treasury has no rules requiring competition in the solicitation of bids, which is the exact opposite of HUD. Despite the fact that local governments receiving Federal funds through HUD for blight elimination may have their own requirements for competition under local law or rule, those local governments must follow HUD’s requirements for competition.

HUD’s requirements for competition flow down to all levels of those receiving Federal dollars, which HUD refers to as “pass-through.”²¹ For example, if a city receives Federal funding under HUD’s blight elimination program, the city must engage in full and open competition, and adhere to the other competition requirements set by HUD, as must all of the city’s contractors and subcontractors. This is true regardless of any local

²⁰ 2 CFR § 200.319.

²¹ See, e.g., 2 CFR §§ 200.318-324.



requirements on competition that may or may not apply.²² HUD is not alone in passing its Federal requirements through to all recipients of Federal funds. The Federal Emergency Management Agency also passes through its Federal requirements to all levels of recipients of its Federal funds.

HUD's requirement for full and open competition generally requires all recipients of Federal funds to use competitive procedures when soliciting contracts under the blight elimination program. HUD established this requirement, "in order to ensure objective contractor performance and eliminate unfair competitive advantage."²³ HUD's requirement for full and open competition:

- Prohibits those who worked on requests for proposals from bidding,
- Prohibits placing unreasonable requirements on firms in order for them to qualify to do business,
- Prohibits noncompetitive pricing practices between firms or between affiliated companies,
- Prohibits organizational conflicts of interest,
- Prohibits specifying only a "brand name" product instead of allowing "an equal" product to be offered and describing the performance or other relevant requirements, and
- Prohibits any arbitration action.

HUD has other pro-competition requirements that establish a hierarchy of the bid solicitation procedures required to be used based on the size of the contract or other factor:²⁴

- HUD generally requires that the work will be **competitively bid out** (\$150,000+).²⁵
- HUD expresses a preference for **sealed bids** (meaning the bid is blind without the company identified). Sealed bidding requires a

²² 2 CFR § 200.38, "Federal Award"; § 200.317, "Procurements by States;" § 200.318, "General Procurement Standards;" § 200.319, "Competition;" and § 200.320, "Methods of Procurement to be Followed." HUD also requires that any pass-through entity (such as a local government) evaluate each sub-recipient's risk of noncompliance with Federal statutes and regulations. 2 CFR § 200.317.

²³ 2 CFR § 200.319.

²⁴ 2 CFR § 200.320.

²⁵ 2 CFR § 200.320.



publicly advertised solicitation of multiple bidders with a sufficient period of time given to respond.²⁶

- When sealed bidding is not feasible, **competitive proposals** can be used to solicit bidders. The competitive proposal method requires soliciting offers from an adequate number of qualified bidders through a public request for proposal that details the specific evaluation factors to be used.²⁷
- **Noncompetitive methods** are considered exceptions, to be used only in limited circumstances. For example, sole source procurement can only be used when the item is available only from a single source, there is a public emergency, a Federal agency expressly authorizes it in writing in response to a written request from a non-Federal entity, or competition is determined to be inadequate after solicitation from a number of sources.²⁸ According to the Office of Management and Budget (“OMB”), noncompetitive contracts are less favored as they carry risks, such as overspending because the contracts have not been negotiated with the benefit of a market mechanism.²⁹
- HUD even requires competition for smaller contracts (less than \$150,000), requiring them to be bid out using a price or rate quote obtained from an adequate number of qualified sources.³⁰
- HUD also requires that recipients take all necessary affirmative steps to assure that **minority and women owned businesses** are used when possible.³¹

In stark contrast, Treasury has no competitive solicitation requirements in TARP’s Hardest Hit Fund Blight Elimination Program. Treasury’s agreements with state agencies are silent on the need for any competition in soliciting bidders for nearly \$622 million in Federal funds for blight elimination. Treasury’s initial, approximately 20-page, base agreement (created in 2009, before the HHF involved blight elimination), has a general catchall provision requiring state agencies to follow all applicable Federal, state and local laws, regulations and guidance. That catchall

²⁶ 2 C.F.R. § 200.320(c).

²⁷ 2 C.F.R. § 200.320(d).

²⁸ 2 C.F.R. § 200.320(f).

²⁹ Office of Management and Budget, “Memorandum for Chief Acquisition Officers Senior Procurement Executives,” October 27, 2009,

https://www.whitehouse.gov/sites/default/files/omb/assets/procurement_gov_contracting/increasing_competition_10272009.pdf, accessed 4/20/2016.

³⁰ 2 C.F.R. § 200.320(b).

³¹ 2 CFR § 200.321.



provision is not sufficient to protect the Federal Government's interest in competition because it is unclear what laws, regulations or guidance Treasury believes applies to these state agencies related to competition. All of the laws specified in Treasury's agreement with the state agencies relate to homeowner rights.³² Treasury never amended this list of laws to specify laws, rules, or guidance that require competition.

Treasury did not follow HUD's lead and establish similar requirements for competition in the solicitation of work in this program. Treasury does not require the state agencies to require local partners to engage in competition in soliciting work.

Treasury does not require that nearly \$622 million in Federal funds for services contracted for under its program will even be bid out at all. Even when the work is bid out, there is no requirement that the competition be full and open. There is no prohibition against receiving a single quote from a sole source. There is no prohibition on placing unreasonable requirements on firms to qualify. There is no preference that bids be sealed. For smaller contracts, there is no requirement to receive quotes from an adequate number of sources. There is no requirement that affirmative steps be taken to use minority and women owned business.

Because there are no Federal requirements, Treasury is not conducting any oversight over whether there is competition in the program. While Treasury conducts oversight through compliance checks, Treasury's compliance staff is checking compliance with Treasury's requirements, not compliance with any state or local requirements. A Treasury requirement is necessary for Federal oversight over competition in this program.

³² The Federal laws included in Treasury's agreement with state HFAs are the Truth in Lending Act, the Home Ownership and Equity Protection Act, the Federal Trade Commission Act, The Equal Credit Opportunity Act, the Fair Credit Reporting Act, the Fair Debt Collection practices Act, the Real estate Settlement Procedures Act, the Fair Housing Act, the Gramm Leach Bliley Act, the Fair and Accurate Credit Transactions Act, "and all other Federal and state laws and regulations applicable thereto, including, without limitation, those designed to prevent unfair, discriminatory or predatory lending practices, tenant rights and licensing."



SIGTARP Found That Without a Treasury Requirement or Guidance to Do So, 6 of the 7 State Agencies Administering Treasury's Blight Elimination Program Have No Requirement for Full and Open Competition for \$590 Million (94% of Federal Funds), and 5 of the 7 State Agencies Have No Competitive Solicitation Requirements for \$560 Million (90% of Federal Funds)

Treasury did not require state agencies to establish requirements for competition in soliciting work and, as a result, 5 of 7 of the state agencies administering Treasury's Blight Elimination Program have no requirements for competitive solicitation. The lack of state agency requirements for competitive solicitation evidences that Treasury's catchall provision requiring state agencies to follow all applicable laws, regulations, or guidance, is not sufficient guidance by Treasury to ensure that competition is required.

Individually, without a Treasury requirement, only one state agency in HHF—HHF South Carolina—has a requirement in its guidelines for “open and free competition.”³³ HHF South Carolina is only authorized to spend \$35 million on blight elimination, which is 6% of total Federal funding under this program. Implementation of this requirement remains to be seen, as HHF South Carolina first began reporting demolitions in May 2016. HHF South Carolina does not have all of the HUD requirements on how the bidding should take place. HHF South Carolina has only one paragraph on competition in its guidelines. The guidelines state that HHF South Carolina will approve procurement policies submitted as part of the application by a local partner, which must include conflict of interest requirements and state a preference for the use of minority and women owned business.

HHF Alabama has no requirement for full and open competition in soliciting work, but only has one competitive solicitation requirement—that there be at least two bids for each property reimbursed under the program. However, HHF Alabama's guidelines do not address other competitive solicitation requirements, such as how contracts should be bid (*e.g.*, sealed bid, competitive proposals). HHF Alabama is only authorized to spend \$25 million on blight elimination, which is 4% of total Federal funding under this program.

³³ SC Housing Corp., “Neighborhood Initiation Program: Guidelines,” provides that all procurements “be conducted in a manner to provide, to the maximum extent practical [sic], open and full competition.” In addition, the guidelines provide that contractor-screening requirements not be so overly “stringent as to prevent the participation of an adequate number of competent contractors.”



The result is that 94% of Treasury's Federal funding committed to blight—nearly \$590 million—has no Federal or state agency requirement for full and open competition in soliciting work. Further, 90% of Treasury's Federal funding for blight elimination—more than \$560 million—has no Federal or state requirement on competition in soliciting work. Missing in these HHF states is any Federal or state requirement for full and open competition and basic, minimum contract solicitation requirements that, for example, dictate the manner in which offers from potential contractors should be solicited and the ways in which such contracts should be bid (*e.g.*, sealed bid, competitive proposals).³⁴

The protections that exist in HUD's blight elimination program that require full and open competition, including competition in the solicitation of work, do not exist in Treasury's Blight Elimination Program, which leaves Treasury's program substantially at risk of fraud, waste, and abuse (see Table 2).

³⁴ HHF Michigan provides a general timeline for creating and publishing "bid packets," with no requirements that address competition. HHF Indiana has a template bid package that references "sealed bids", but has no requirement that local partners use this bid package or use sealed bids.



Table 2: Competition Requirements for Solicitation in HUD's NSP and Treasury's Blight Elimination Program

Competition Requirement	HUD in NSP	States, Municipalities & Other Recipients in HUD NSP (Applying Federal requirements)	Sub-Recipients in HUD NSP (Applying Federal requirements)	Treasury in the HHF Blight Elimination Program	State Agencies in the HHF Blight Elimination Program	Recipients in the HHF Blight Elimination Program
Full and open competition	✓	✓	✓		1 of 7 states (6% of funding)	Inconsistent or nonexistent
Prohibition on unreasonable requirements to qualify	✓	✓	✓			Inconsistent or nonexistent
Prohibition on noncompetitive pricing practices	✓	✓	✓			Inconsistent or nonexistent
Contracts over \$150,000 to be competitively bid	✓	✓	✓			Inconsistent or nonexistent
Sealed bid	✓	✓	✓			Inconsistent or nonexistent
If sealed bid not feasible, competitive proposals from an adequate number of qualified bidders through a public request for proposal	✓	✓	✓			Inconsistent or nonexistent
Noncompetitive methods only under narrow exceptions	✓	✓	✓			Inconsistent or nonexistent
Smaller contracts (less than \$150,000), bid out for quote obtained from an adequate number of qualified sources	✓	✓	✓			Inconsistent or nonexistent
Efforts for Minority and women owned businesses	✓	✓	✓		1 of 7 states (6% of funding)	Inconsistent or nonexistent

Note: HHF Alabama only has one competitive solicitation requirement—that there be at least two bids for each property reimbursed under the program—in its guidelines, which do not address other competitive solicitation requirements, such as how contracts should be bid (e.g., sealed bid, competitive proposals).

Sources: 2 C.F.R. §§ 200.318-326; participating state HFAs' HHF Participation Agreements with Treasury (as amended); participating state HFAs' HHF program guidelines; and the procurement policies and procedures of selected program partners.



Without Any Federal Requirement to Do So, 6 of 7 State Agencies in HHF Have No Requirements for Competition That Apply to Local Partners Awarding Contracts for \$590 Million (94% of Federal Funds)

SIGTARP found that 6 of 7 state HFAs also have no requirements for competition that apply to local partners awarding contracts for the work under this Federal program. As a result, with the limited exception of HHF South Carolina, those who receive Federal funds get to decide how to award contracts with no Federal requirements governing these decisions.

This is in stark contrast to HUD's requirements (see Table 3). HUD's requirements that pass through to all recipients include:³⁵

- Among other things, all non-Federal entities receiving financial assistance from HUD must establish written procedures that: (1) clearly and accurately describe the technical requirements in a way that does not unduly restrict competition; and (2) identify all requirements that the bidders must fulfill; and (3) identify all factors to be used in evaluating bids or proposals.
- All non-Federal entities are prohibited from using statutorily or administratively imposed state, local, or tribal geographical preferences in the evaluations of bids or proposals.
- All non-Federal entities must ensure that all prequalified list of companies are current and include enough qualified sources to ensure maximum open and free competition, and must not preclude potential bidders from qualifying during the solicitation period.

In addition, when sealed bidding is used, HUD requires that bids be evaluated without discussions with the bidders, and that a firm fixed price contract be awarded to the **lowest bidder** who satisfies the terms and conditions of the solicitation. When competitive proposals are used, HUD generally permits discussions or negotiations between the government and offerors, and requires that either a fixed or a cost-reimbursement contract be awarded to the vendor whose proposal is **most advantageous** to the program. HUD has also developed templates incorporating the major NSP solicitation requirements to help non-Federal entities meet HUD's requirements.

³⁵ 2 C.F.R § 200.319.



Table 3: Competition Requirements for Contract Awards in HUD's NSP and Treasury's Blight Elimination Program

Competition Requirement	HUD in NSP	States, Municipalities & Other Recipients in HUD NSP (applying Federal requirements)	Sub-Recipients in HUD NSP (applying Federal requirements)	Treasury in the HHF Blight Elimination Program	State Agencies in the HHF Blight Elimination Program	Recipients in the HHF Blight Elimination Program
Written procedures that describing the technical requirements in a way that does not unduly restrict competition	✓	✓	✓			Inconsistent or nonexistent
Written procedures that identify all requirements that bidders must fulfill	✓	✓	✓		1 of 7 states (6% of funding)	Inconsistent or nonexistent
Written procedures that all factors to be used in evaluating bids or proposals	✓	✓	✓			Inconsistent or nonexistent
Prohibitions against geographical preferences in the evaluations of bids or proposals	✓	✓	✓			Inconsistent or nonexistent
Ensure that all prequalified list of companies are current and include enough qualified sources to ensure maximum open and free competition	✓	✓	✓			Inconsistent or nonexistent
Prohibition against precluding potential bidders from qualifying during the solicitation period	✓	✓	✓			Inconsistent or nonexistent
Sealed bids: award to lowest bidder who satisfies the terms and conditions of the solicitation	✓	✓	✓			Inconsistent or nonexistent
Competitive proposals: award to vendor whose proposal is most advantageous to the program	✓	✓	✓			Inconsistent or nonexistent

Sources: 2 C.F.R. §§ 200.318-326; participating state HFAs' HHF Participation Agreements with Treasury (as amended); participating state HFAs' HHF program guidelines; and the procurement policies and procedures of selected program partners.



The protections that exist in HUD's blight elimination program that require competition in the awarding of work do not exist in Treasury's Blight Elimination Program, which leaves Treasury's program substantially at risk of fraud, waste, and abuse.

Unlike HUD's Blight Elimination Program, Treasury and HHH State Agencies Let Those Receiving Federal Funds (87% of Which Are Not Public Entities) Set the Rules and Procedures for Competition, Leaving TARP Vulnerable to Fraud, Waste, and Abuse

SIGTARP found that unlike HUD, Treasury and state agencies running this TARP program allow the recipients of Federal funds to decide whether to have competition and in what form. Treasury's Blight Elimination Program leaves it up to local partners to decide whether and how to advertise or bid out demolition and other contracts, and how to award contracts.³⁶ By leaving competition up to those receiving Federal funds rather than those in charge of the program, Treasury's program is extremely vulnerable to fraud, waste, and abuse.

State agency requirements that local partners follow all state or local applicable laws is not sufficient to protect against serious risks in this program, as HUD has determined. First, this leads to inconsistent and at times, non-existent, requirements for competition. Second, even if local requirements apply, they may not be as strong as HUD's requirements.³⁷

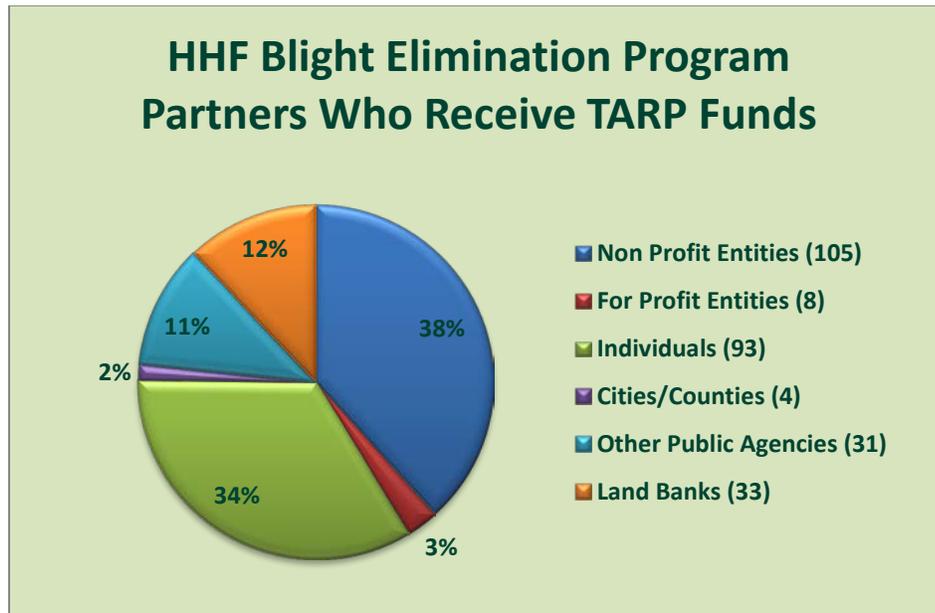
Third, most of the local partners may not even be subject to state or local competition requirements as 87% are not municipalities or public agencies. Of the nearly 280 local partners who are receiving Federal HHH Blight Elimination Funds; there are nearly 100 individuals, 8 for-profit companies, 105 non-profit entities, and 33 land banks.

³⁶ Only one HHH state (HHF Illinois) requires recipients to certify that contracts comply with applicable municipal procurement policies and procedures. This reliance on policies and procedures that may or may not apply, which may be inconsistent and weaker than HUD's requirements, is not sufficient to protect the program.

³⁷ SIGTARP found no Treasury or state guidelines that show how Treasury and the state HFAs will bring accountability to ensure that local laws on competition are followed, with one limited exception. HHH South Carolina's guidelines require program recipients and partners to submit procurement policies for the HFA's approval prior to approving them to participate in HHH Blight Elimination. But these guidelines and the remaining other HHH state guidelines do not address the state agency bringing accountability by determining whether local laws or rules were followed.



Figure 1: HHF Blight Elimination Program Partners Who Receive TARP Funds



Source: SIGTARP analysis of state HFA responses to SIGTARP request.

Many of these partners may not be subject to any oversight over competitive requirements that might apply. Even if these local partners are subject to local requirements on competition, many may have limited knowledge or experience in competition requirements or competitive practices. Additionally, each may be subject to different (or no) procurement rules at the local and/or state level.

Without Federal requirements on competition, SIGTARP found that the HHF Blight Elimination Program has a patchwork of contracting rules and practices that may or may not apply and that may not provide the same protections as Federal laws and rules that apply in HUD's blight elimination program, NSP. HUD did not rely on a patchwork of local laws or rules that might be applicable. This patchwork situation increases the risk that local partners and their subcontractors may award contracts based on self-interest, favoritism, or use non-competitive practices that lead to inflated costs or other inefficiencies, or fraud, waste, and abuse, rather than ensuring that all TARP contracts reflect the benefits and protections of competition to the maximum extent practicable.

SIGTARP found that the local partners in Treasury's program award contracts using a patchwork of differing standards and procedures. SIGTARP found considerable differences across and among local partners as to whether they had any formal procedures at all and, where such policies existed, as to what they required. Some have adopted their own



policies, which may or may not conform to local standards. Other local partners do not identify any policies on contract awards.

In comparison to HUD's blight elimination program, Treasury's Blight Elimination Program is plagued by a patchwork of inconsistent—or even non-existent—local contracting standards, rules, and practices, leaving the program at great risk of fraud, waste, and abuse, and with substantially fewer protections than HUD's program.

Public Policy Interests Support Treasury Protecting This Program to the Same Extent as HUD's Program By Requiring Full and Open Competition and Other Competition Standards for the Remaining Hundreds of Millions of Federal Dollars Still Available

Treasury can require full and open competition and other competition standards to promote the same public policy interests and protect against the same risks that are present in HUD's blight elimination program. The time is right for Treasury to protect this program by requiring competition. Four state agencies are just getting started with blight elimination under HHF, and are not yet reporting any demolitions. Treasury has recently expanded the program, announcing an additional \$2 billion for the Hardest Hit Fund, with some of those funds for blight elimination. In April, Treasury announced additional HHF allocations without identifying the use for those funds—so it appears that more Federal funds are likely to be allocated in the future for blight elimination.

There are significant policy reasons for Treasury protecting this program to the same extent as HUD. Competition is a cornerstone principle in the Federal Government. The Administration and Treasury have publicly discussed public policy interests that support maximizing competition. In 2009, President Obama called on Federal agencies to maximize the use of full and open competition and other competitive processes with the goal of minimizing risk and maximizing the value of Government contracts.³⁸ In guidance calling for immediate action to increase competition in contracting, the Administration laid out the public interest for competition stating:

³⁸ The White House, "Memorandum for the Heads of Executive Departments and Agencies - Subject: Government Contracting," March 4, 2009, <https://www.whitehouse.gov/the-press-office/memorandum-heads-executive-departments-and-agencies-subject-government-contracting>, accessed 4/20/2016.



“Competition lies at the heart of the federal acquisition system. It drives down costs, motivates better contractor performance, helps to curb fraud and waste, and promotes innovation.”³⁹

Treasury recognizes the public interests of competition as it has adopted similar requirements as HUD for Treasury’s grants, Federal awards and cooperative agreements.⁴⁰ Treasury states on its website:

“...to ensure reasonable prices, contracts are awarded competitively whenever possible. This practice reflects the theory that full and open competition results in fair and reasonable prices and that such competition avoids favoritism by assuring that all qualified suppliers have the opportunity to sell to the government.”⁴¹

The HHF Blight Elimination Program has no Federal requirements to harness the benefits and protections of competition in soliciting offers from potential contractors. Fair and reasonable prices, better contract performance, and innovation are public policy interests that should be promoted in this TARP program.

Treasury’s Program for Blight Elimination Is Far More at Risk than HUD’s Program for Blight Elimination Given the Absence of Federal Requirements on Competition

SIGTARP found that Treasury’s program suffers from many of the same risks present in HUD’s program without the same protections. HUD recognized risks in its blight elimination program and took effort to protect against those risks by including Federal requirements on competition. According to Treasury, the HHF Blight Elimination Program is not a grant program. Federal regulations on competition like those that apply in HUD’s blight elimination program do not apply to Treasury’s program. This position ignores the fact that HHF is a Federal program funded with taxpayer dollars. The substantive risks to the program based on the services and work being provided should dictate the protections needed, over the formal designation of the funds. These risks do not go

³⁹ Office of Management and Budget, “Memorandum for Chief Acquisition Officers Senior Procurement Executives,” October 27, 2009, https://www.whitehouse.gov/sites/default/files/omb/assets/procurement_gov_contracting/increasing_competition_10272009.pdf, accessed 4/20/2016.

⁴⁰ See 2 C.F.R. § 1000.10. Treasury does not consider HHF Blight Elimination funding to be a grant, Federal award, or cooperative agreement.

⁴¹ Treasury, “Part 1: Basic Contracting Principles,” <https://www.treasury.gov/about/organizational-structure/offices/Mgt/Pages/dcfo-osdbu-how-to-part1-03-contracting.aspx>, accessed 4/20/2016.



away just because Treasury chooses not to address them. However, Treasury has not created its own requirements for competition.

Treasury has left the program at substantial risk that recipients of Federal dollars may restrict competition. There is risk that recipients may fail to make reasonable efforts to get proposals from enough eligible sources, put unreasonable requirements on bidding that result in severely curtailing competition, fail to publicize solicitations in a way most favorable to competition, favor specific companies through an overly short response window, or improperly exclude contractors from the pool of potential offerors. The absence of Treasury requirements on competition also leaves Treasury's Blight Elimination Program at risk of not obtaining the most competitive contract prices, of awarding contracts to contractors with improper conflicts of interest, and excluding participation by minority and women-owned businesses.

SIGTARP found that the lack of a Federal requirement for full and open competition (and other competition requirements) also makes this program extremely vulnerable to fraud, waste, and abuse. Federal rules on competition are supposed to keep Federal programs fair. Fairness is critical to preserving public trust in Federal agencies conducting oversight over these programs. Very serious harms may seep into this Federal program. Favoritism, undue influence, contract steering, bid-rigging, and other closed-door contracting processes, can result from a lack of Federal requirements on competition and Federal oversight to ensure compliance with those requirements. All of these increase the risk of fraud, self-dealing, waste, and even corruption.



Conclusion

SIGTARP found that the Federal government funds two main programs for the demolition of blighted houses, but only the U.S. Department of Housing and Urban Development's ("HUD") program has Federal requirements to protect the Government against substantial risks inherent in contracting for demolition work—Treasury's Hardest Hit Fund does not. SIGTARP found that blight elimination under Treasury's Hardest Hit Fund lacks very basic Federal requirements that govern HUD's blight elimination program. While TARP-funded demolition of abandoned houses has great potential benefit to communities, the absence of Federal requirements specific to the risks inherent in blight elimination like those that exist in HUD's blight elimination program puts Treasury's program at great risk of fraud, waste, and abuse. At least one city mayor seeking funds under Treasury's program stated publicly that these funds come with no stipulations—a perception that will only change when Treasury creates Federal stipulations to mitigate substantial risk. Right now, the risks of HHF blight elimination continue unregulated and unchecked for more than half a billion Federal dollars.

Treasury followed HUD's lead in creating a Federally-funded blight elimination program, but made its program bigger (nearly \$622 million compared to HUD's \$300 million) and without blight-specific Federal requirements designed to protect against the risks inherent in this activity. While Treasury conducted a written analysis of the benefits of expanding HHF to include blight elimination, there is no Treasury written analysis of the risks. It should have been obvious to Treasury that demolition activities and the flow of Federal dollars through hundreds of individuals, companies, and other non-Federal entities carry far greater risk to the Federal Government than providing Federal funds to unemployed or at-risk homeowners, which had previously been HHF's sole activity. Treasury could have used HUD as a model for Federal requirements needed to mitigate risks inherent in blight elimination, but it did not—instead only amending its contract with participating state agencies with 2-3 pages of provisions in large type that are insufficient to protect against risks inherent to contracting for demolition and other activities.

Treasury's Hardest Hit Fund program is significantly vulnerable to the substantial risks of unfair competitive practices and overcharging, either of which could lead to fraud, waste, and abuse. The most glaring difference between the two Federal blight programs is that HUD requires: (1) full and open competition (and other competition requirements); and (2) that demolition and other costs must be necessary and reasonable. Treasury requires neither.



Treasury's program is at far greater risk than HUD's program given that Treasury has zero Federal requirements for competition. Unlike Treasury, HUD does not leave competition to chance. Without similar requirements to HUD, Treasury is not conducting any oversight over whether there is competition in the solicitation or awarding of Federal funds or whether costs are necessary and reasonable. This means that more than half a billion in Federal dollars contracted with nearly 280 local partners, each who may have contractors and subcontractors, is being expended with zero Federal requirements for competition, and no requirement that demolition costs be necessary and reasonable.

There is a substantial public interest in having Federal requirements for competition in this TARP program. Federal requirements for competition are designed to keep programs fair. The Administration has said that competition drives down costs, motivates better contractor performance, helps curb fraud and waste, and promotes innovation. Favoritism, undue influence, contract steering, bid-rigging, and other closed-door contracting processes, can result from a lack of Federal requirements for competition.

There is no harm in Treasury creating Federal requirements for full and open competition, and other competition requirements, similar to HUD's program. HUD's program allows for the same locally-tailored solutions and flexibility that Treasury seeks, only with accountability and oversight not present in HHF, and with less risk of fraud, waste, and abuse. HUD protects the Federal Government and the program through 6 pages in small font of Federal requirements for competition, requirements that flow down to state and local governments. By contrast, in the face of Treasury's silence, the state agencies administering Treasury's program have no requirements for full and open competition in this program, with one very small exception. One small agency in South Carolina, which is allocated 6% of total funding for TARP blight elimination, requires "open and free" competition, leaving 94% of this program (nearly \$590 million in Treasury funding) with no requirement for full and open competition. Clearly, HHF South Carolina has determined that there is no harm in requiring full and open competition, just as there would be no harm to the remaining \$590 million in funding through six other HHF state agencies. Beyond HHF South Carolina's single paragraph on competition, HHF Alabama (which is allocated 4% of TARP funding for blight elimination) has a single sentence in its guidelines on competition (requiring two bids), evidencing that there is no harm in competition.

Those running this program (Treasury and state agencies) are essentially allowing the recipients of Federal funds to determine whether to have competition and in what form. This has led to a patchwork of inconsistent



or non-existent practices on competition. Treasury does not require that nearly \$622 million in Federal funds will even be bid out at all. Treasury does not require that competition be full and open, prohibit a single quote from a sole source, or prohibit placing unreasonable requirements on firms to qualify. Two small HHF state agencies are the only ones in this program even attempting to set any requirements for competition, which is insufficient to protect nearly \$622 million.

Unlike Treasury, HUD does not allow the recipient of Federal dollars to set the rules on competition, but instead layers on any state or local laws or rules that might apply on top of Federal requirements. Unlike HUD, Treasury's program relies exclusively on state/city laws or rules. Local rules may not even apply to the nearly 280 local partners in Treasury's program because most (87%) of them are not municipalities or public agencies, but instead include nearly 100 individuals, 8 for-profit companies, 105 non-profit entities, and 33 land banks. Any rules that may apply are varied, leaving the Federal Government substantially at risk compared to HUD's blight elimination program.

SIGTARP also found that HUD limits Federal dollars for blight elimination to only necessary and reasonable costs, but Treasury does not, leaving HHF at risk of overcharges, waste, and fraud. Treasury has a cap of \$25,000 or \$35,000 per property, which is not sufficient to protect the Federal Government from paying for costs that are not necessary and reasonable. Treasury's cap far exceeds the average cost of demolition, reflective of worst-case-scenarios. Treasury's Blight Elimination Program is leaving the analysis of what is necessary and reasonable to the recipients of Federal funds. HUD does not place such trust or hope in recipients to protect the Federal government.

At the very least, Treasury's program should have the same protection as the other Federally-funded blight elimination program. The requirements of a grant program (at HUD) should be the bare minimum for a TARP program. HHF does not have to be a grant for Treasury to protect it. That would be form over substance. Federal grant funds are not the only Federal funds that should be protected. TARP funds are bailout funds that Congress designed to be accompanied by accountability. TARP funds should have more accountability and oversight than grant programs. Treasury should make its own requirements to protect the program.

The Hardest Hit Fund is a homeowner bailout program fought for by Congress, which rejected TARP at first. It is not a bailout of cities, no matter how good the intentions, or developers, construction companies, non-profits, for-profits, land banks, or individuals who are not at-risk homeowners. This program has a lot of self-interests involved and with



that come risks and vulnerabilities that need strong protection— protection that exists in HUD's program, but not in Treasury's program.

TARP funds for demolitions of abandoned properties were taken from programs that directly gave TARP money to homeowners, primarily in the form of unemployment and underemployment assistance. Every dollar that pays a demolition contractor for costs that are not necessary or reasonable is a dollar taken away from a homeowner. Every dollar that pays a demolition contractor for costs that are not necessary or reasonable is a dollar taken away from demolishing an abandoned house that causes safety concerns for a neighborhood. That is why it is so important that Treasury create Federal rules to protect this program and these bailout funds, and why it is so important that everyone with oversight of TARP keeps this new use of TARP for razing homes tightly focused and protected.



Recommendations

1. Treasury should assess in writing all potential risks associated with demolition and other blight elimination activities under the Hardest Hit Fund. Treasury's analysis should include, but not be limited to, potential risks related to a lack of competition for blight elimination activities, and payments for demolition and other costs that are not necessary or reasonable.
2. Treasury should implement a comprehensive set of Federal requirements to mitigate risks associated with blight elimination activities and the contracting for those activities.
3. Treasury should require full and open competition for the hundreds of millions of TARP dollars available in the Hardest Hit Fund for blight elimination, and make that requirement pass through the layers of funding and reimbursement.
4. Treasury should prohibit those who worked on requests for proposals from bidding on blight elimination work under the Hardest Hit Fund, and make that requirement pass through the layers of funding and reimbursement.
5. Treasury should prohibit placing unreasonable requirements on firms in order to have them qualify to do business related to the Hardest Hit Fund's blight elimination activities, and make that requirement pass through the layers of funding and reimbursement.
6. Treasury should prohibit noncompetitive pricing practices between firms or affiliated companies for blight elimination work under the Hardest Hit Fund, and make that requirement pass through the layers of funding and reimbursement.
7. Treasury should generally require that blight elimination work under the Hardest Hit Fund be competitively bid out, and make that requirement pass through the layers of funding and reimbursement.
8. Treasury should express a preference for the use of sealed bids for blight elimination work under the Hardest Hit Fund, and make that requirement pass through the layers of funding and reimbursement.
9. When sealed bidding is not feasible, Treasury should require the use of competitive proposals for blight elimination work under the



Hardest Hit Fund. Treasury should require soliciting offers from an adequate number of qualified bidders through a public request for proposal that details the specific evaluation factors to be used. Treasury should make these requirements pass through the layers of funding and reimbursement.

10. Treasury should only allow noncompetitive methods of solicitation for blight elimination work under the Hardest Hit Fund in rare exceptions, and should delineate those exceptions. Treasury should prohibit receiving a single quote from a single source. Treasury should make these requirements pass through the layers of funding and reimbursement.
11. Treasury should require that recipients of blight elimination funding under the Hardest Hit Fund take all necessary affirmative steps to assure that minority and women owned businesses are used when possible. Treasury should make these requirements pass through the layers of funding and reimbursement.
12. Treasury should require that all non-Federal entities or individuals contracting for blight elimination work under the Hardest Hit Fund establish written procedures that: (1) clearly and accurately describe the technical requirements in a way that does not unduly restrict competition; (2) identify all requirements that bidders must fulfill; and (3) identify all factors to be used in evaluating bids. Treasury should make these requirements pass through the layers of funding and reimbursement.
13. Treasury should require that all prequalified lists of companies and individuals for blight elimination work under the Hardest Hit Fund are current and include enough qualified sources to ensure maximum open and free competition, and prohibit the preclusion of potential bidders from qualifying during the solicitation period. Treasury should make these requirements pass through the layers of funding and reimbursement.
14. Treasury should require that when sealed bids are used, that bids are evaluated without discussion of the bidders, and that a firm fixed price contract be awarded to the lowest bidder who satisfied the terms and conditions of the solicitation. Treasury should make these requirements pass through the layers of funding and reimbursement.
15. Treasury should require that when competitive proposals are used for blight elimination work under the Hardest Hit Fund, that either a fixed or a cost-reimbursement contract be awarded to the



vendor whose proposal is most advantageous to the program. Treasury should make this requirement pass through the layers of funding and reimbursement.

16. Treasury should conduct oversight to ensure compliance with all of its requirements related to competition for blight elimination under the Hardest Hit Fund.
17. Treasury should limit costs to be reimbursed by Hardest Hit Fund dollars to only those demolition or other blight elimination activity costs that are necessary and reasonable.
18. Treasury should require state housing finance agencies involved in blight elimination under the Hardest Hit Fund to conduct a written analysis of what demolition and other related costs are necessary and reasonable in each city or county, and provide that analysis to Treasury. To conduct this written analysis, Treasury should require the state housing finance agencies to follow best practices including using independent experts, obtaining third party fair market price quotes, and obtaining established practices and policies regarding current and historical cost information on Federal, state, and local blight elimination, particularly by the same parties conducting blight elimination activities under the Hardest Hit Fund. Treasury should require that state housing finance agencies keep this analysis current.
19. Treasury should require state housing finance agencies involved in blight elimination under the Hardest Hit Fund to conduct due diligence necessary for effective review of claims for Federal funds by benchmarking all submitted claims against the written analysis prepared by the state housing finance agency. Treasury should require the state housing finance agencies to engage in higher scrutiny by requiring substantial justification for invoices that exceed the cost in the written analysis, and that state agencies provide a written analysis of its scrutiny of the submitted justification.
20. Treasury should conduct oversight to ensure compliance with all of its requirements limiting reimbursement of blight elimination costs to only those that are necessary and reasonable.



Management Comments and SIGTARP's Response

Treasury provided comments to the draft report. SIGTARP addressed those comments where applicable. Treasury generally disagreed with SIGTARP's findings citing to the expertise of states and need for states' flexibility, an issue that SIGTARP has addressed in the audit. Treasury did not agree to implement SIGTARP's recommendations, but said it would consider them.



Appendix A – Objectives, Scope, and Methodology

SIGTARP performed this audit under authority of Public Law 110-343, as amended, which also incorporates the duties and responsibilities of inspectors general under the Inspector General Act of 1978, as amended. We initiated this audit as part of our continuing oversight of TARP. The specific objective of this audit was to consider risk factors that could impact the effectiveness of the Hardest Hit Fund (“HHF”) Blight Elimination Program.

As of June 1, 2016, Treasury had approved the allocation of nearly \$622 million in TARP funds from HHF homeowner assistance programs to the HHF Blight Elimination Program to demolish and “green” vacant and abandoned single and multifamily residential structures. The scope of this audit covered the 7 state Housing Finance Agencies (“HFAs”) participating in HHF that Treasury had approved for the Blight Elimination Program: Alabama, Michigan, Ohio, Illinois, Indiana, South Carolina and, most recently, Tennessee. Our work covered the period from June 2013 through June 2016.

SIGTARP conducted interviews with and obtained program documentation from officials at Treasury and the participating state HFAs, along with selected local blight program partners and/or recipients who perform HHF Blight Elimination Program activities.

SIGTARP reviewed and analyzed data from the participating state HFAs and their program partners, to include state Housing Participation Agreements, the HFAs quarterly performance reports, the HFAs program guidelines, and demolition, “greening” and other contracts. In addition, SIGTARP reviewed press releases related to blight elimination, and Treasury’s and the state HFAs’ websites for information related to the HHF Blight Elimination Program. SIGTARP also reviewed and analyzed the U.S. Department of Housing and Urban Development’s requirements in its blight elimination programs.

SIGTARP conducted the audit from March 2015 through June 2016 in Washington, D.C.; Detroit, Michigan; Lansing, Michigan; Flint, Michigan; Indianapolis, Indiana; Columbus, Ohio; and Cleveland, Ohio. Our audit was conducted in accordance with generally accepted government auditing standards established by the U.S. Government Accountability Office. Those standards require that SIGTARP 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. SIGTARP



believes that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Limitations on Data

SIGTARP generally relied on Treasury, the state HFAs, and their blight elimination program partners to provide relevant documentation, including email communications and other files related to the HHF Blight Elimination Program. To the extent that the documentation provided to SIGTARP by these entities did not reflect a comprehensive response to SIGTARP's documentation requests, SIGTARP's review may have been limited.

Use of Computer-Processed Data

To perform this audit, SIGTARP relied on data provided by Treasury and the state HFAs. Specifically, SIGTARP relied on Treasury's and the state HFAs' quarterly performance reports to determine the numbers and percentages of structures demolished and the median costs for demolition and other activities. SIGTARP did not validate the accuracy of the data.

Internal Controls

To assess internal controls pertaining to the HHF Blight Elimination Program, SIGTARP interviewed state HFA and program partner officials; reviewed applicable state HFA independent auditor reports on internal controls; and reviewed policies and procedures from Treasury, the participating state HFAs and selected program partners to determine the extent to which internal controls were reasonable and effective.

Prior Coverage

SIGTARP has covered the HHF Blight Elimination Program in its quarterly reports since January 2015, and in two audit reports. On April 21, 2015, SIGTARP issued an audit report, "Treasury Should Do Much More to Increase the Effectiveness of the TARP Hardest Hit Fund Blight Elimination Program." SIGTARP also issued an alert letter on December 14, 2015, that addressed a risk related to diverting TARP funds to demolish lived-in properties, which could undermine the success of HHF's Blight Elimination Program. In addition, SIGTARP reviewed audit work performed by the Government Accountability Office and HUD's Office of Inspector General as it relates to blight elimination activities.



Appendix B – Acronyms and Abbreviations

CDBG	Community Development Block Grant
EESA	Emergency Economic Stabilization Act
HAMP	Home Affordable Modification Program
HFAs or state HFAs	Housing finance agencies
HHF	Housing Finance Agency Innovation Fund for the Hardest Hit Housing Markets (also “Hardest Hit Fund”)
HUD	U.S. Department of Housing and Urban Development
NSP	Neighborhood Stabilization Program
OMB	Office of Management and Budget
TARP	Troubled Asset Relief Program
Treasury	U.S. Department of the Treasury



Appendix C – Audit Team Members

This audit was conducted and the report was prepared under the direction of Jenniffer F. Wilson, Deputy Special Inspector General for Audit and Evaluation, and Christopher Bosland, Assistant Deputy Special Inspector General for Audit and Evaluation, Office of the Special Inspector General for the Troubled Asset Relief Program.

Staff members who conducted the audit and contributed to the report include Vonda Batts, Yusuf House, Yvonne Monyei, Katherine McCall, William Saunders, Tracy Davis-Ross, Stefanie Holloway, David White, and Joshua Alexander.



Appendix D – Management Comments



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

June 15, 2016

The Honorable Christy G. Romero
Special Inspector General
for the Troubled Asset Relief Program
1801 L Street, NW, 4th Floor
Washington, DC 20036

Dear Ms. Romero:

I write in response to the Special Inspector General for the Troubled Asset Relief Program's (SIGTARP) draft report of June 1, 2016 (Draft). The Office of Financial Stability (OFS) thanks you for conducting this review and looks forward to working with SIGTARP as we continue to support the programs under the Housing Finance Agency (HFA) Innovation Fund for the Hardest Hit Housing Markets (HHF). This letter provides OFS's official response to the Draft. Pursuant to our customary protocol, we will review all of SIGTARP's recommendations and respond to each one under separate cover at a later date.

I. HHF Background and the Successes in the Blight Elimination Program.

HHF is one of the housing programs created under the Troubled Asset Relief Program (TARP) pursuant to the Emergency Economic Stabilization Act of 2008 (EESA). Specifically, it was created in February 2010 to provide aid to the District of Columbia and 18 states designated "hardest hit" because they had experienced the nation's steepest home price decline and most severe unemployment. HHF provides the greatest possible flexibility to eligible HFAs in designing programs that are responsive to the needs of their specific states. The HFAs design, administer, and monitor their own HHF programs, subject to requirements set forth in the contracts they signed with Treasury.

The state HFAs have designed and currently operate 80 distinct programs under HHF, each with their own unique objectives, processes and requirements. Seven states have implemented programs devoted to blight elimination, with the goal of preventing avoidable foreclosures and stabilizing housing markets in surrounding communities. The Draft incorrectly states that OFS repurposed HHF funds to include blight elimination. All funds provided under HHF are for the purpose of preventing foreclosures and stabilizing housing markets. It is the state HFAs that design programs and seek to create and implement the blight elimination programs.

The HFAs have seen successes in administering their blight elimination programs under HHF. As the Draft notes, HHF funds have been used to remove 9,293 blighted residential structures as of December 31, 2015. Those actions are already achieving significant results. In Detroit, for example, a recent study found that each HHF demolition increased the value of homes within



500 feet by 4.2 percent.¹ According to the study, these demolitions, together with other targeted state and local initiatives, have increased property values in HHF zones by up to 13.8 percent. The study also estimated that for every HHF dollar spent on blight elimination, neighboring homeowners realized \$4.27 in increased home equity. We look forward to further positive results as the state HFAs continue to implement their programs.

II. HHF's Protections and Controls to Prevent Fraud, Waste, and Abuse.

OFS takes very seriously its responsibility to monitor state HFAs, and requires that each state implement internal controls designed to minimize the risk of fraud, mitigate conflicts of interest, and maximize operational effectiveness. OFS assesses the HFAs' compliance with Treasury's requirements through regular on-site compliance reviews, which test the effectiveness of internal controls and functions – including underwriting activities, program disbursements, administrative expenses, financial reporting, and other control functions. In addition, HFAs are required to provide OFS with an independent verification of the effectiveness of their internal control program on an annual basis.

OFS has modified its monitoring of state HFAs in response to the introduction of blight elimination programs. For example, OFS has required the development of metrics to measure the performance of HHF blight elimination programs and their effect on target markets, adjusted its quarterly reporting templates to account for blight elimination data, and established monthly calls for HHF states with blight elimination programs to share best practices. In response to a SIGTARP recommendation, OFS issued guidance to HFAs that clarified that properties could not be legally occupied at the time of review or approval for blight elimination activity.

OFS has also tailored its compliance approach to address the specific risks and requirements of blight elimination programs. OFS's on-site compliance visits include internal control assessments and reviews of the states' systems and processes to administer their blight elimination programs. On a sample basis, OFS verifies that properties selected for demolition satisfy the state's eligibility criteria, examines pre- and post-demolition evidence that state processes are being followed, and reviews contractor invoices and other documentation to support the states' disbursement of HHF funds. HFAs may only use HHF funds for actual costs incurred and agreed upon under the contracts they entered into with their partners. In addition, they may disburse HHF funds only upon receipt of documentation that the work has been satisfactorily completed. Through its on-site compliance visits, OFS reviews payments and relevant documentation to validate that these procedures are followed, and that costs are valid and properly supported.

In addition to Treasury's contractual requirements, state HFAs have enumerated more detailed requirements in their respective program guidelines. For example, to help ensure that blight elimination costs are reasonable, every HFA that administers a blight elimination program has specified eligible and ineligible expenses within its program guidelines. Each HFA also requires costs to be itemized and invoiced in order to be eligible for reimbursement. OFS's site visits

¹ "Estimating Home Equity Impacts from Rapid, Targeted Residential Demolition in Detroit, MI: Application of a Spatially-Dynamic Data System for Decision Support," July 2015, retrieved at <http://www.demolitionimpact.org/download/>.



include an assessment of whether HFAs are adhering to their blight elimination program guidelines.

The Draft also discusses the value of competitive bidding for funds under blight elimination programs. We note that HFAs have used both competitive and direct-partnering strategies to expeditiously accomplish the goals of their programs. Most states with HHF blight elimination programs have employed a competitive application process to select partners and allocate HHF funds. In other cases, states have directly selected experienced partners – such as land banks – to leverage the already-established infrastructure for blight elimination available in the state.

III. SIGTARP's Draft Compares HHF to non-TARP Housing Programs.

The Draft discusses some procedures that the U.S. Department of Housing and Urban Development (HUD) follows in its own blight elimination program, the Neighborhood Stabilization Program (NSP). OFS recognizes the importance of preventing fraud, waste, and abuse, and agrees with the spirit of these recommendations. We note, however, that there are key differences between NSP and HHF, and that these differences should be kept in mind when comparing the programs.

Treasury currently provides HHF funds to seven states with blight elimination programs, and does so in a way that is tailored to the needs and circumstances of those states. By contrast, NSP provides its funds to a much wider range of recipients—250 local governments and all 50 states—and does so subject to the same standardized regulations as the still-broader Community Development Block Grant program (CDBG). Moreover, while HHF was intended to address dire local conditions in the jurisdictions hardest hit by the economic crisis, NSP and CDBG are targeted at a wide range of long-term objectives.

The Draft also states that the costs of demolition under HHF may be higher than under non-HHF blight elimination programs. We note that state HHF programs generally allow for costs related to acquisition, demolition, greening and maintenance, and have different standards for the work that is performed. Because non-HHF programs may have had different standards or acceptable expenditures from those associated with HHF blight elimination programs, these differences make it difficult to compare financial results among the programs.

IV. Conclusion

As noted above, we believe the fundamental structure of HHF and the existing controls and compliance measures implemented by OFS and the HFAs have made HHF blight elimination programs effective, flexible, and accountable. OFS appreciates SIGTARP's analysis, and is closely examining its recommendations. We strongly believe that preventing fraud, waste, and abuse is critical to the success of any government program. We look forward to working with SIGTARP as we monitor the housing programs under TARP and continue to wind down our various programs. In connection with our review, we will consult with other knowledgeable



government agencies to analyze whether further changes are necessary. We will respond to each recommendation under separate cover after careful consideration.

Sincerely,

A handwritten signature in blue ink, appearing to read "Mark McArdle".

Mark McArdle
Deputy Assistant Secretary for Financial
Stability



SIGTARP Hotline

If you are aware of fraud, waste, abuse, mismanagement, or misrepresentations associated with the Troubled Asset Relief Program, please contact SIGTARP.

By *Online Form*: www.SIGTARP.gov
2009

By *Phone*: Call toll free: (877) SIG-

By *Fax*: (202) 622-4559

By *Mail*: **Office of the Special Inspector General
for the Troubled Asset Relief Program**
1801 L Street., NW, 3rd Floor
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