

AUDIT AND FINANCE COMMITTEE MEETING BOOK OF JUNE 27, 2019



**Sharon Thomason, Chair
Paul Braden, Member
Asusena Reséndiz, Member
Leo Vasquez, III, Member**

**TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS
AUDIT AND FINANCE COMMITTEE MEETING**

**AGENDA
7:30 AM
June 27, 2019**

**John H. Reagan Building
JHR 140, 105 W 15th Street
Austin, Texas 78701**

CALL TO ORDER

ROLL CALL

Sharon Thomason, Chair

CERTIFICATION OF QUORUM

The Audit and Finance Committee of the Governing Board of the Texas Department of Housing and Community Affairs (TDHCA) will meet to consider and may act on any of the following:

ACTION ITEMS:

- ITEM 1:** Presentation, discussion, and possible action to approve the Audit and Finance Committee Minutes Summary for March 21, 2019
- ITEM 2:** Presentation, discussion, and possible action on the FY 2020 Operating Budget
- ITEM 3:** Presentation, discussion, and possible action on the FY 2020 Housing Finance Division Budget

Mark Scott
Director of
Internal Audit
Ernie Palacios
Director of Financial
Administration

REPORT ITEMS:

- ITEM 1:** Presentation and discussion of Internal Audit of the Construction Cost Certification function
- ITEM 2:** Report on the status of the external audit activities

Mark Scott
Director of
Internal Audit

**PUBLIC COMMENT ON MATTERS OTHER THAN ITEMS FOR WHICH THERE WERE POSTED
AGENDA ITEMS**

EXECUTIVE SESSION

The Committee may go into Executive Session (close its meeting to the public) on any agenda item if appropriate and authorized by the Open Meetings Act, Tex. Gov't Code, Chapter 551 and under Tex. Gov't Code, §2306.039.

Pursuant to Tex. Gov't Code, §551.074 the Audit Committee may go into Executive Session for the purposes of discussing personnel matters including to deliberate the appointment, employment, evaluation, reassignment, duties, discipline, or dismissal of a public officer or employee.

Pursuant to Tex. Gov't Code, §551.071(1) the Committee may go into executive session to seek the advice of its attorney about pending or contemplated litigation or a settlement offer.

Pursuant to Tex. Gov't Code, §551.071(2) the Committee may go into executive session for the purpose of seeking the advice of its attorney about a matter in which the duty of the attorney to the governmental body under the Texas Disciplinary Rules of Professional Conduct of the State

Bar of Texas clearly conflicts with Tex. Gov't Code, Chapter 551.

Pursuant to Tex. Gov't Code, §2306.039(c) the Committee may go into executive session to receive reports from the Department's internal auditor, fraud prevention coordinator, or ethics advisor regarding issues related to fraud, waste, or abuse.

OPEN SESSION

If there is an Executive Session, the Committee will reconvene in Open Session and may take action on any items taken up in Executive Session. Except as specifically authorized by applicable law, the Audit Committee may not take any actions in Executive Session.

ADJOURN

To access this agenda and details on each agenda item in the board book, please visit our website at www.tdhca.state.tx.us or contact Mark Scott, TDHCA Internal Audit Director, 221 East 11th Street Austin, Texas 78701-2410, 512-475-3813 and request the information.

Individuals who require auxiliary aids, services or sign language interpreters for this meeting should contact Terri Roeber, ADA Responsible Employee, at 512-475-3959 or Relay Texas at 1-800-735-2989, at least five days before the meeting so that appropriate arrangements can be made.

Non-English speaking individuals who require interpreters for this meeting should contact Elena Peinado, 512-475-3814, at least five days before the meeting so that appropriate arrangements can be made.

Personas que hablan español y requieren un intérprete, favor de llamar a Elena Peinado, al siguiente número 512-475-3814 por lo menos cinco días antes de la junta para hacer los preparativos apropiados.

NOTICE AS TO HANDGUN PROHIBITION DURING THE OPEN MEETING OF A GOVERNMENTAL ENTITY IN THIS ROOM ON THIS DATE:

Pursuant to Section 30.06, Penal Code (trespass by license holder with a concealed handgun), a person licensed under Subchapter H, Chapter 411, Government Code (handgun licensing law), may not enter this property with a concealed handgun.

De acuerdo con la sección 30.06 del código penal (ingreso sin autorización de un titular de una licencia con una pistola oculta), una persona con licencia según el subcapítulo h, capítulo 411, código del gobierno (ley sobre licencias para portar pistolas), no puede ingresar a esta propiedad con una pistola oculta.

Pursuant to Section 30.07, Penal Code (trespass by license holder with an openly carried handgun), a person licensed under Subchapter H, Chapter 411, Government Code (handgun licensing law), may not enter this property with a handgun that is carried openly.

De acuerdo con la sección 30.07 del código penal (ingreso sin autorización de un titular de una licencia con una pistola a la vista), una persona con licencia según el subcapítulo h, capítulo 411, código del gobierno (ley sobre licencias para portar pistolas), no puede ingresar a esta propiedad con una pistola a la vista.

NONE OF THESE RESTRICTIONS EXTEND BEYOND THIS ROOM ON THIS DATE AND DURING THE

**MEETING OF THE AUDIT COMMITTEE OF THE TEXAS DEPARTMENT OF HOUSING AND
COMMUNITY AFFAIRS.**

Action Item

1

AUDIT AND FINANCE COMMITTEE ACTION REQUEST

INTERNAL AUDIT DIVISION

June 27, 2019

Presentation, discussion and possible action on Audit and Finance Committee Meeting Minutes Summary for March 21, 2019

RECOMMENDED ACTION

RESOLVED, that the Audit and Finance Committee Meeting Minutes Summary for March 21, 2019 are hereby approved as presented.

**MINUTES OF THE AUDIT AND FINANCE COMMITTEE MEETING
OF THE GOVERNING BOARD OF THE
TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS**

On Thursday, March 21, 2019, at 7:30 a.m. the meeting of the Audit and Finance Committee (the "Committee") of the Governing Board (the "Board") of the Texas Department of Housing and Community Affairs ("TDHCA" or the "Department") was held in the Dewitt C. Greer State Highway Building, Ric Williamson Hearing Room, 125 East 11th Street, Austin, Texas. Sharon Thomason presided over the meeting, and Mark Scott served as secretary. Committee members Paul A. Braden, Leo Vasquez, and Asusena Resendiz were in attendance and represented a quorum for the committee meeting.

The first action item on the agenda was approval of the minutes of the December 6, 2018 meeting of the Committee. Minutes were adopted as presented, and were approved.

The second action item was the review and possible acceptance of the State auditor's Office (SAO) audit of the TDHCA Financial Statement, and was presented by Ms. Puerto from SAO. Sarah Puerto introduced herself as the project manager for the audit of TDHCA FY 18 financial statement. She stated that SAO issued several reports as part of this audit; including the email communication on December 20, 2018 which included a document entitled Required Communication with Those Charged with Governance, and that included several items that SAO is required to communicate to the Board. Ms. Puerto then offered to answer any questions that the Committee members may have. With no questions Ms. Thomason asked for a motion to recommend approval of the SAO's audit to the full Board. Motion was passed unanimously. That concluded the action items.

Three report items were on the agenda, with first one being the Internal Audit report of the Public Information Request, or PIR, function. Mr. Scott, Director of Internal Audit, presented the report. He stated that the agency has processes to ensure compliance with the Public Information Act. There were some recommendations for fine-tuning some of the processes, and ways to categorize large and complicated requests. In response to this audit the division has updated its Standard Operating Procedures (SOP). With no questions regarding PIR audit Mr. Scott moved to the next report item; Internal Audit review of TDHCA's licensing, inspection and outreach for migrant labor housing.

Mr. Scott stated that for this review internal audit staff visited five of the licensed facilities and some of the worksites. The visit went well and the owners / operators of the licensed facilities were very cooperative. Auditors reviewed the records of the inspections and the outreach activities, and made recommendations in regard to the point of contact for the MOU between TDHCA and MH, and different ways that the inspection processes and the record keeping can

be improved. TDHCA receives \$250 fee for each license application. We recommended better accounting and tracking for the time and travel spent on the inspections.

At the conclusion Mr. Scott offered to answer questions for the Committee members. Ms. Resendiz asked about the selection of the five facilities that were visited. Mr. Scott responded that the selection was to include a good sample of different facilities. Couple of the facilities was in close proximity to Austin, two were in the Valley, and one by San Antonio.

Mr. Vasquez asked whether the locations visited were off-season, and if so that would require a mini follow up. Mr. Scott replied that there's a caveat in the report for that reason and that the facilities visited looked good but it was not during the growing season or when the weather is hot. He also added that he would be glad to go out again during the harvest season. In respond to Mr. Vasquez's question regarding the cost of administering the program Mr. Scott said that from cost accounting standpoint we're not capturing the full cost of running this program. Mr. Vasquez added that his concern is that we have an unfunded mandate from the legislature to administer this program but without enough resources to actually make it happen.

Mr. Cabello, director of Program Oversight and Controls, offered additional comments. He talked about some of the issues and challenges facing the migrant farm workers program, such as the increased number of licensed facilities which are inspected by MH. As the number of licenses increasing it's becoming harder for MH to continue inspecting them. Also the \$250 per license doesn't cover all the costs associated with the time spent on the inspection and the related matters. There are several bills that are going through the process right now that may affect the inspection and administration of this program.

Mr. Vasquez asked about the possible total universe of the licenses / facilities, to which Mr. Cabello answered that there are many different figures out there in Texas. USDA does the census of agricultural workers every five years and the last census from 2012 had identified just fewer than 4900 migrant farm workers in Texas. It has also been stated in several meetings that a large percentage of the migrant farm workers are undocumented. Mr. Vasquez said that he would imagine the number to be more like 49,000 than 4,900. Mr. Cabello agreed. He also shared some of the new efforts and initiatives the agency has taken to reach out to the farm workers and facility operators.

Mr. Cabello said that the operators are not required to provide housing to the migrant farm workers. In regard to housing standards he said that there are two standards, one followed by TWC and one by TDHCA. TWC standard is lower than TDHCA depending on the year the facility was built.

Ms. Resendiz asked about the TDHCA's outreach to partners and how the information is being communicated to them. Mr. Cabello said that we're communicating with organizations who

work with migrant farm workers in addition to a 1-800 number that migrant farm workers can use to report any issue or problems with the facilities. This information is gathered and reported to TDHCA by MH. In the last several years only two complaints have been reported. With the new outreach effort it is expected that the numbers of reports will increase, which in turn means more expense and manpower needs for the agency.

Mr. Cervantes, acting executive director for TDHCA, added that they agree with auditor's recommendation in expanding the tracking of time and expenses that's taking place. Currently the operating budget for this program is \$10,250 in general review. TDHCA has been trying to leverage the work that MH is doing in the region in an effort to minimize costs and MH has been very generous with their manpower. They're being reimbursed for primarily travel costs. Mr. Cervantes also added that one modification that was included in the recent legislative appropriations request was to modify the type of financing that is in the bill and to move it into "Appropriated receipt", which is more of a fee generation type of funding. This request is still in process. This should help the agency continue the program, increase the fee generation, and create the balance in this program that the auditors are recommending. Currently there are bills on both side of this issue and we've had discussions and we've served as resources thus far to convey our thoughts on the matter. We had a proposed rule related to this activity a while back which we then put on hold because we wanted to see what might surface during this session and then blend that back into our policy in terms of our rule.

Mr. Resendiz expressed her appreciation for the work that has been done in bringing more light to this program. Mr. Cabello added that he's working with office of representative Romero who has been in contact with USDA to provide an additional report that will capture more information on migrant farm workers. This should give us more data in reference to migrant farm workers.

With no other questions Ms. Thomason moved to the final report item which was an update on the status of the 2019 internal audit plan and was presented by Mr. Scott.

Mr. Scott said that the plan is moving along on schedule, and the next audit to start is the internal audit of Performance Measures at the agency, and also the audit of Construction Cost Certification function of multifamily division.

Ms. Thomason asked if there were any public comments. With no other questions or comments the meeting was adjourned at 7:55am.

Action Item

2

AUDIT AND FINANCE COMMITTEE ACTION REQUEST

FINANCIAL ADMINISTRATION DIVISION

JUNE 27, 2019

Presentation, discussion, and possible action on the FY 2020 Operating Budget

RECOMMENDED ACTION

WHEREAS, the Governing Board of the Texas Department of Housing and Community Affairs (the Department or TDHCA) is required to approve a FY 2020 Operating Budget; and

WHEREAS, the Department is required to submit the budget to the Governor's Office and the Legislative Budget Board (LBB); and

WHEREAS, the Department is required to establish the salary of the Executive (or Acting) Director;

NOW, therefore, it is hereby

RESOLVED, that the FY 2020 Operating Budget, in the form presented to this meeting, is hereby approved; and

RESOLVED, that the Board approves a salary for the Executive (or Acting) Director up to and including the amount budgeted for the position in Article VII of the 2020-2021 General Appropriations Act (GAA)

FURTHER RESOLVED, that upon approval by the TDHCA Governing Board, the Department will submit the budget to the Governor's Office and the LBB; and

FURTHER RESOLVED, that J.B. Goodwin, Board Chair, be and he hereby is authorized and empowered, for and on behalf of this Board, to establish the salary of the Executive (or Acting) Director subject to the provisions of the 2020-2021 GAA; and

FURTHER RESOLVED, that the Department will submit written notice of any action taken by the Board regarding salary of the Executive (or Acting) Director to the Governor's Office, the LBB, and the Comptroller.

BACKGROUND

In accordance with Tex. Gov't Code Chapter 2306, TDHCA is charged with preparing an operating budget for Board adoption on or before September 1 of each fiscal year. The budget includes

operational expenses distributed among the Department's divisions. It does not include federal or state program funds that pass through to subrecipients except for administrative funds used by the Department associated with those federal or state funds that are retained and reflected in the budget. This budget anticipates maximizing all federal administrative resources. In addition, in accordance with internal auditing standards and the Board's internal audit charter, the budget includes the Internal Audit Division's annual operating budget.

This FY 2020 Internal Operating Budget, which the Board is being asked to approve, corresponds to the first year of the biennial GAA passed by the 86th Texas Legislature which appropriated \$287,263,052. In total, this budget provides for expenditures and associated revenues of \$27,727,986 or a \$268,099 (1.0%) decrease from the prior year budget.

The budget reflects 311 Full Time Equivalent (FTEs) (64 are related to the Manufactured Housing Division) which is two less than appropriated.

Additionally, the Housing Finance Division budget, which is funded with fees generated from the Department's Bond, Housing Tax Credit, Asset Management, and Compliance activities, decreased by \$51,734 or -0.3%. This decrease is primarily attributed to the Capital Budget and advertising expenses.

For a complete explanation of the aforementioned budget categories and details, please see the accompanying Comparison Report.

TEXAS DEPT. OF HOUSING AND COMMUNITY AFFAIRS

FY 2020 Operating Budget

Comparison Report

June 27, 2019

This Comparison Report provides an explanation of some of the changes to cost categories.

In total, this FY 2020 Operating Budget is \$27,727,986 or a \$268,099 (1.0 %) decrease over the prior year budget. Below are the highlights of the FY 2020 Budget. Please refer to the "Comparison by Expense Object" schedule on Page 4.

1. **Salaries/Wages and Payroll Related Costs.** These two line items represent 83% of the total operating budget.

The budget reflects 311 Full Time Equivalents ("FTEs").

The Salaries and Wages line item increased by \$358,295 or 2.0%. This total increase from 2019 is primarily due to the normal growth rate of 1% and the addition of 2 FTEs, as well as the legislatively approved increase to the Executive Director position. The two new FTEs are a result of the addition of 1 FTE each in the Multifamily and Subrecipient Monitoring sections. One FTE was repurposed from the Fair Housing, Data Management, and Reporting section to the Section 8 program.

Payroll related costs increased \$85,991. The increase in payroll related costs is proportional to the increase in salaries.

2. **Out of State Travel.** Out of State Travel increased by \$16,010. This increase is in the areas of Compliance, Program Controls, Bond Finance, Multifamily, and Community Affairs. The average costs for out of state trips has increased as well as the need for staff to attend trainings and conferences such as National Council of State Housing Agencies (NCSHA) semi-annual conferences offered across the US and bond pricings.
3. **Professional Fees.** Professional Fees have increased by \$289,421 related to the need for an expanded contract for inspection services. There is a substantial anticipated increase in Compliance Physical Inspections due to changed IRS regulations. Additionally, there is a need for outsourcing of Section 8 inspections due to more comprehensive inspection requirements imposed by the Department of Housing and Urban Development (HUD). There is also an increase in professional fees for the Community Affairs division for ongoing updates related to a database that was part of the Capital Budget in FY18 and FY19.

4. ***Repairs/Maintenance.** Repairs and Maintenance decreased by \$121,805 primarily due to lower computer related annual maintenance costs.
5. **Rentals and Leases.** Rentals and leases decreased by \$22,774 due to a decreased demand for paid rental locations for meetings and trainings.
6. **Materials and supplies.** Materials and supplies increased by \$9,964 due to an agency wide increase in cost of consumable supplies such as toner and related materials.
7. **Advertising.** Agency advertising costs decreased \$79,700 or 47.9%. The decrease in advertising costs is due to the conclusion of a FY19 marketing initiative by the Texas Homeownership Division. This cost is not part of the FY20 budget.
8. **Temporary Help.** Temporary Help decreased \$28,630. The decrease in this category is primarily due to the removal of a web redesign of the Texas Homeownership Programs for the new year. The initial cost of \$45,000 was included in the FY19 budget but for FY20 and moving forward there will be an ongoing maintenance cost of \$10,000 per year. However there was also an increase in the cost of the agency security services.
9. ***Furniture and Equipment.** Included in this category is the Legislature's approval of the Department's Hardware and Software Replacements project as it relates to non-capital expenses associated with the Department's Capital Projects, such as update and replacement of end-user computers and operational software upgrades, including the replacement of desktop computers (75) and laptops (96) that will be six years old or older and software updates. The benefits of these planned purchases include increased security, better performance for end-user computers, and the ability to provide continued support for TDHCA's enterprise systems, such as the Central Database, PeopleSoft Financials, MITAS Financials/Servicing, and the Manufactured Housing System.

This line item increased \$226,528 due to an anticipated increase in capital expenditures for items such as computers and printers, the majority of which will occur in the first year of the biennium.

10. ***Capital Outlay.** This category is also included in the Department's Legacy System Modernization Project as it relates to capital expenses such as server hardware upgrades and network equipment enhancements, to ensure systems remain supported by vendors and security and reliability remain at high levels. In FY19 this section included the People Soft financials Centralized Accounting and Payroll/Personnel System ("CAPPS") upgrade of \$200,000, and the Cyber Security Project of \$180,000 – of which \$80,000 was moved forward from FY18 to FY19 for continued expenditures. New software needed by the Community Affairs division costing \$600,000 was originally budgeted in FY18 but has also been moved to FY19 for continued work on this project. Capital Outlay decreased \$1,007,600 due to the items mentioned above that are no longer in the agency's budget for FY20.

**The Department's Capital Projects are included in Repairs/Maintenance, Furniture and Equipment and Capital Outlay. These projects include hardware and software replacements, ongoing CAPPs financials license fees, and the Disaster recovery services through the data center services performed by the Department of Information Resources.*

Comparison by Expense Object

	2019 Budget (a)	2020 Budget (b)	Variance (b-a)	Percentage Change
Salaries and Wages	\$ 18,130,352	\$ 18,488,647	\$ 358,295	2.0%
Payroll Related Costs	4,351,285	4,437,275	85,991	2.0%
Travel In-State	538,732	547,900	9,168	1.7%
Travel Out-of-State	125,394	141,404	16,010	12.8%
*Professional Fees	1,222,098	1,511,518	289,421	23.7%
Material and Supplies	273,542	283,506	9,964	3.6%
*Repairs/Maintenance	731,680	609,876	(121,805)	-16.6%
Printing and Reproduction	16,247	23,597	7,350	45.2%
Rentals and Leases	158,101	135,327	(22,774)	-14.4%
Membership Fees	84,582	86,930	2,348	2.8%
Staff Development	147,500	148,850	1,350	0.9%
Insurance/Employee Bonds	409,174	408,101	(1,072)	-0.3%
Employee Tuition	8,000	7,000	(1,000)	-12.5%
Advertising	166,350	86,650	(79,700)	-47.9%
Freight/Delivery	27,350	20,950	(6,400)	-23.4%
Temporary Help	158,580	129,950	(28,630)	-18.1%
*Furniture and Equipment	49,250	275,778	226,528	460.0%
Communication and Utilities	366,286	360,900	(5,386)	-1.5%
*Capital Outlay	1,007,600	-	(1,007,600)	-100.0%
State Office of Risk Management	23,981	23,826	(154)	-0.6%
Total Department	27,996,084	\$ 27,727,986	\$ (268,099)	-1.0%

* Budget categories that include Capital Budget items

FTE's	309	311	2.00	0.6%
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Method of Finance:

General Revenue:

GR-General Revenue	\$ 810,708	\$ 816,670	\$ 5,962	0.7%
GR-Earned Federal Funds	2,206,653	2,310,063	103,410	4.7%
Federal Funds-Non-HERA	6,959,086	6,829,706	(129,380)	-1.9%
Federal Funds-Neighborhood Stabilization Program (HERA)	114,790	115,130	339	0.3%
Appropriated Receipts - Housing Finance	17,024,184	16,972,451	(51,734)	-0.3%
Appropriated Receipts - Manufact. Housing	512,645	512,296	(349)	-0.1%
Interagency Contracts	368,017	171,672	(196,345)	-53.4%
Total, Method of Finance	\$ 27,996,084	\$ 27,727,986	\$ (268,099)	-1.0%

Note: Appropriated Receipts - Housing Finance include Bond Administration Fees, Housing Tax Credit Fees, Asset Management Fees, Compliance Fees, and Migrant Labor Housing Fees.

Methods of Finance

The 2020 Budget includes the following sources:

General Revenue

State appropriated funds including Housing Trust Fund, Housing and Health Services Coordinating Council, Homeless Housing and Services Program,.

Earned Federal Funds - Federal funds appropriated for indirect costs associated with administering federal funds.

Federal Funds

Federal Funds-(Non-Housing and Economic Recovery Act (“HERA”)) - Core federal programs such as Community Services Block Grant, Emergency Solutions Grant, HOME, U.S. Dept. of Energy (“DOE”), Section 8 Housing, Section 811 PRA Program, Low Income Home Energy Assistance Program, and National Housing Trust Fund.

Neighborhood Stabilization Program - Federally appropriated funds specifically designated for HERA-NSP.

Appropriated Receipts - Housing Finance (“HF”):

Bond Admin Fees - Appropriated receipts associated with our Single Family and Multifamily bond programs such as application fees, issuance fees, and administration fees.

Low Income Housing Tax Credit Fees - Appropriated receipts associated with our housing tax credit program such as application fees and commitment fees.

Compliance Fees - Fees assessed to multifamily developers for the purpose of ensuring long-term compliance.

Asset Oversight Fees - Fees assessed to Tax Credit Assistance Program (“TCAP”) and Exchange property owners for the purpose of safeguarding the Department’s financial interest in their properties.

Migrant Labor Housing Fees – Fees assessed for the purpose of inspections of migrant housing facilities.

Appropriated Receipts (MH) - Manufactured Housing Division fees generated through inspecting, licensing, and titling activities.

Interagency Contracts - Contract with the Texas Department of Agriculture for the Office of Colonia Initiatives (“OCI”) Self-Help Center’s operation and administration; and a potential contract still in negotiation with HHSC for Home and Community-Based Services-Adult Mental Health Program (“HCBS-AMH”), a program that supports individuals with mental illnesses.



FISCAL YEAR 2020
OPERATING BUDGET
(September 1, 2019 through August 31, 2020)

June 27, 2019

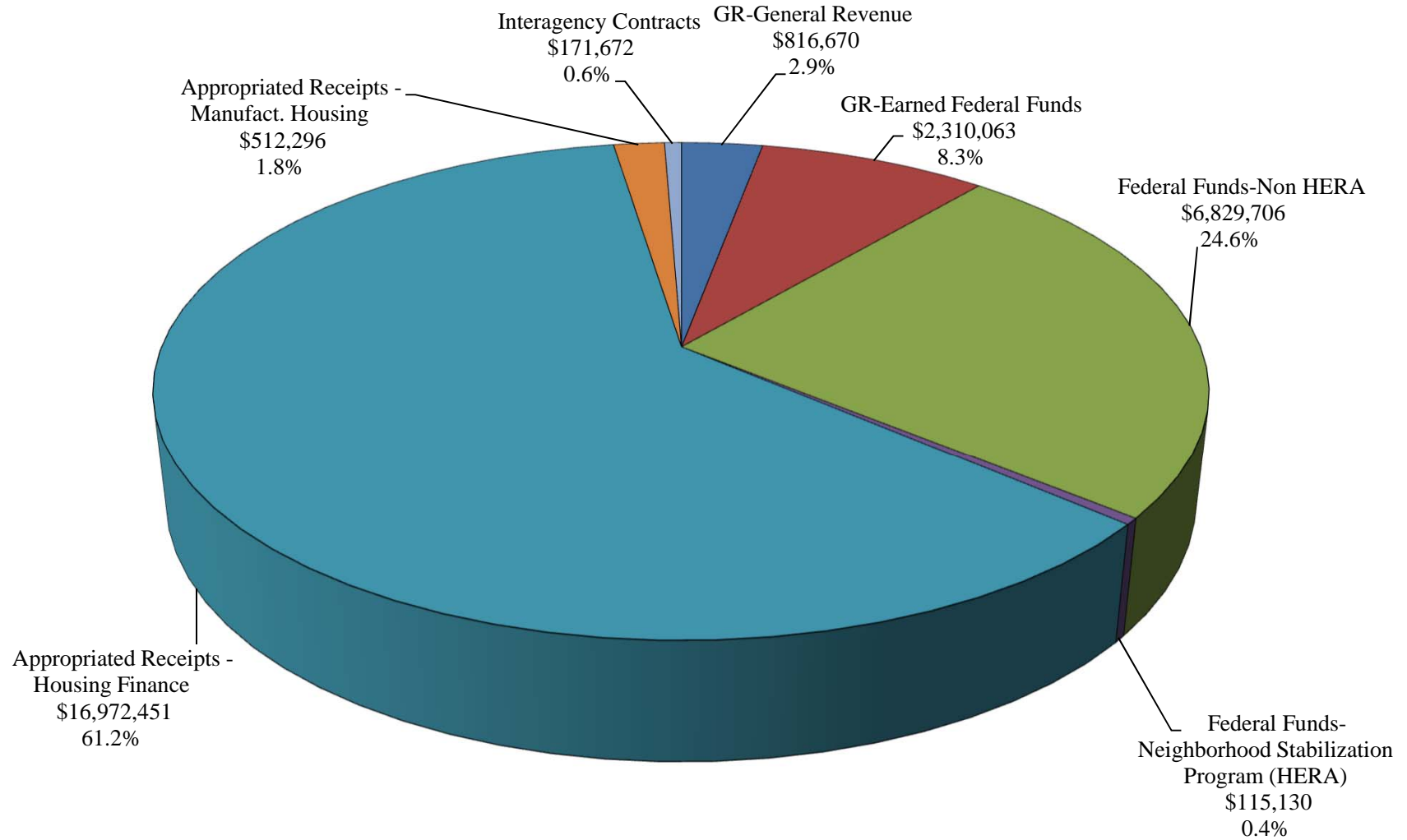
Prepared by the Financial Administration Division

**TEXAS DEPARTMENT OF HOUSING AND
COMMUNITY AFFAIRS FY-2020 OPERATING BUDGET**

T A B L E O F C O N T E N T S

Method of Finance Chart..... 1
Agency Wide – By Method of Finance..... 2

Texas Department of Housing and Community Affairs FY 2020 Method of Finance



Total Budget: \$27,727,986

Agency Wide - By Method of Finance

September 1, 2019 thru August 31, 2020

Budget Categories	MH					Total
	General Revenue	Federal Funds	Appropriated Receipts	Interagency Contract	Appropriated Receipts	
Salaries	2,086,778	4,676,000	11,192,669	128,282	404,919	18,488,647
Payroll Related Costs	595,645	1,063,682	2,649,980	30,788	97,181	4,437,275
Travel In-State	32,700	192,190	313,010	10,000	-	547,900
Travel Out-of-State	4,364	40,975	96,065	-	-	141,404
Professional Fees	63,628	534,718	913,172	-	-	1,511,518
Materials/Supplies	56,944	37,946	188,616	-	-	283,506
Repairs/Maintenance	114,156	60,086	435,633	-	-	609,876
Printing and Reproduction	3,266	4,871	15,459	-	-	23,597
Rental/Lease	23,200	17,312	94,815	-	-	135,327
Membership Dues	1,814	25,069	60,047	-	-	86,930
Staff Development	13,958	49,670	85,222	-	-	148,850
Insurance/Employee Bonds	61,162	76,776	257,565	2,402	10,196	408,101
Employee Tuition	3,241	-	3,759	-	-	7,000
Advertising	38	2,563	84,049	-	-	86,650
Freight/Delivery	986	1,820	18,144	-	-	20,950
Temporary Help	16,417	20,470	93,063	-	-	129,950
Furniture/Equipment	2,259	77,257	196,063	200	-	275,778
Communications/Utilities	40,523	62,553	257,823	-	-	360,900
Capital Outlay	-	-	-	-	-	-
State Office of Risk Management	5,653	878	17,296	-	-	23,826
Total	3,126,734	6,944,835	16,972,451	171,672	512,296	27,727,986
Budget by Method of Finance, 2019	3,017,361	7,073,876	17,024,184	368,017	512,645	27,996,084
Variance from 2019	109,372	(129,041)	(51,734)	(196,346)	(349)	(268,098)

Action Item

3

AUDIT AND FINANCE COMMITTEE ACTION REQUEST

FINANCIAL ADMINISTRATION DIVISION

JUNE 27, 2019

Presentation, discussion, and possible action on the FY 2020 Housing Finance Division Budget

RECOMMENDED ACTION

WHEREAS, the Governing Board of the Texas Department of Housing and Community Affairs (the Department or TDHCA) is required to approve a FY 2020 Housing Finance Division Budget; and

WHEREAS, the Department is required to submit the budget to the Governor's Office and the Legislative Budget Board (LBB);

NOW, therefore, it is hereby

RESOLVED, that the FY 2020 Housing Finance Division Budget, in the form presented to this meeting, is hereby approved; and

FURTHER RESOLVED, that upon approval by the TDHCA Governing Board, the Department will submit the budget to the Governor's Office and the LBB.

BACKGROUND

In accordance with Tex. Gov't Code §2306.113, the Department shall create a separate annual budget for the Housing Finance Division to certify the housing program fee revenue that supports the Department. While at the time the statute was created such a division existed, the duties associated with the Housing Finance Division have been spread among multiple divisions in the agency as reorganizations to improve efficiency have occurred. This budget is a subset of the whole operating budget and shows the Housing Finance revenues also known as Appropriated Receipts that support the operating budget.

This FY 2020 Housing Finance Division Budget, which the Board is being asked to approve, is \$16,972,451. The Housing Finance Budget complies with the provisions of the General Appropriations Act (GAA).

In addition, in accordance with Tex. Gov't Code §§2306.117 and 2306.118, the Department incurs operational and nonoperational expenses in carrying out the functions of the Housing Finance Division. These types of expenses may be paid only from revenues

or funds provided under this Chapter. The revenue and funds of the Department received by or payable through the programs and functions of the Housing Finance Division, other than funds necessary for the operation of the Housing Finance Division and appropriated funds, shall be administered outside the treasury with the Texas Treasury Safekeeping Trust Company.



Housing Finance Budget Appropriated Receipts

September 1, 2019 thru August 31, 2020

Budget Categories	Program						Payroll Related Costs	Total
	Executive Administration	Agency Administration	Program Controls and Oversight	Bond Finance	Programs	Capital Budget		
Salaries	1,567,709	2,882,215	4,323,831	930,122	1,488,792		11,192,669	
Payroll Related Costs	-	-	-	-	-		2,649,980	
Travel In-State	50,675	7,924	208,350	21,500	24,560		313,010	
Travel Out-of-State	29,794	6,336	18,200	23,200	18,535		96,065	
Professional Fees	112,654	248,042	445,429	51,608	18,517	36,923	913,172	
Materials/Supplies	21,121	64,465	63,151	14,964	24,916		188,616	
Repairs/Maintenance	27,817	128,046	162,453	48,415	35,561	33,341	435,633	
Printing and Reproduction	2,189	2,775	2,383	6,050	2,063		15,459	
Rental/Lease	6,777	50,604	18,106	12,591	6,737		94,815	
Membership Dues	49,253	2,658	6,611	1,350	175		60,047	
Staff Development	10,675	23,604	29,665	10,200	11,077		85,222	
Insurance/Employee Bonds	31,481	75,647	103,494	18,972	27,970		257,565	
Employee Tuition	-	3,759	-	-	-		3,759	
Advertising	1,500	113	-	82,000	437		84,049	
Freight/Delivery	1,617	2,404	9,220	4,600	303		18,144	
Temporary Help	34,259	15,302	14,601	18,186	10,715		93,063	
Furniture/Equipment	6,500	6,829	5,565	1,800	2,113	173,256	196,063	
Communications/Utilities	34,944	58,517	90,433	43,337	30,592		257,823	
Capital Outlay	-	-	-	-	-	-	-	
State Office of Risk Management	1,592	6,752	5,877	965	2,110		17,296	
Total	1,990,557	3,585,992	5,507,368	1,289,859	1,705,175	243,520	2,649,980	16,972,451

Method of Finance:

Single Family Bond Administration Fees	1,677,409
Multifamily Bond Administration Fees	535,892
Compliance Fees	3,717,392.52
Housing Tax Credit Fees	2,386,772.01
Asset Management Fees	482,774
Subtotal:	8,800,239
Central Support Single Family Bond Administration Fees	736,879
Central Support Multifamily Bond Administration Fees	1,359,564
Central Support Compliance Fees	3,153,788
Central Support Housing Tax Credit Fees	2,315,412
Central Support Asset Management Fees	606,569
Subtotal:	8,172,212
Total, Method of Finance	16,972,451

Report Item

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AUDIT AND FINANCE COMMITTEE REPORT ITEM

INTERNAL AUDIT DIVISION

June 27, 2019

Presentation and discussion of the Internal Audit of the Construction Cost Certification function

TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS
An Internal Audit of the Construction Cost Certification
Audit Report # 19-004

Executive Summary

The Office of Internal Audit (OIA) reviewed TDHCA's Construction Cost Certification function and its policies, procedures, and controls that are currently in place. Based on our reviews and testing the Asset Management has appropriate processes in place for the Construction Cost Certification function. We've identified some area for improvement, as described in the detailed report.

Findings, Observations, and Recommendations

- OIA recommends that Asset Management require developers to verify CPA firm's licenses validity, including any restrictions, before hiring the firm to perform the audit
- OIA Recommends that management consider establishing rules where the marketing Analysis and the CPA firm performing construction cost certification are not the same entity

Response:

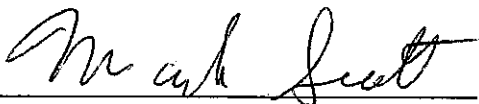
Management agreed with our recommendations, and detailed responses are included in the body of the audit report.

Responsible Area:

Director of Asset Management

Objective, Scope and Methodology

Our scope included a review of the IRS §42, TDHCA's QAP, Asset Management's internal control policies and procedures, as well as other applicable rules and regulations as they apply to LIHTC and Construction Cost Certification processes. Based upon our preliminary understanding of the Construction Cost Certification function we identified critical points and risk, to develop audit objectives and an audit program including methodology. The Texas Internal Auditing Act, Tex. Gov't Code §2102.005 requires testing of the controls of a state agency's major programs and systems, and the controls related to them.



Mark Scott, CPA, CIA, CISA, CFE, MBA
Director, Internal Audit

6/19/2019
Date Signed



TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS

www.tdhca.state.tx.us

Greg Abbott
GOVERNOR

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June 19, 2019

Writer's direct phone # 512.475.3813
Email: mark.scott@tdhca.state.tx.us

Board Members of the Texas Department of Housing and Community Affairs ("TDHCA")

RE: INTERNAL AUDIT REVIEW OF THE CONSTRUCTION COST CERTIFICATION FUNCTION

Dear Board Members:

This report presents the results of the Office of Internal Audit ("OIA") Review of the Construction Cost Certification function. This audit was included in the Fiscal Year 2019 Annual Audit Plan and was conducted in accordance with applicable audit standards. The Construction Cost Certification activity was identified during the 2019 Fiscal Year risk assessment due to its complexity of transactions and recent changes in management.

We reviewed the Asset Management Division's activities related to IRS§42 and Tax Credit certificates. Our scope included a review of the TDHCA's 2018 Qualified Allocation Plan (QAP), IRC section 42, and review of internal controls related to administration and processing of Construction Cost Certification documents and issuance of Tax Credit certificates. Based upon our preliminary understanding of the Construction and Cost Certification function, we identified critical points and risks, and developed our audit objectives and audit plan including methodology.

The amount of certified costs of a project determines the amount of tax credit funds which will be generated over a period of ten years. Therefore the cost certification process is a critical control for the Low Income Housing Tax Credit (LIHTC) program. We reviewed a report by the federal Government Accountability Office (GAO), dated September 2018. The GAO report described a nation-wide study of LIHTC costs, and other aspects of the program. According to the GAO report, Texas has the lowest cost per unit of the states reviewed.



Background

The IRC §42 Low Income Housing Tax Credit (LIHTC) was enacted by Congress as part of the Tax Reform Act of 1986 to encourage new construction and rehabilitation of existing buildings as Low-income rental housing for households within income at or below specified income levels. Under this act investors and developer are given incentives to make equity investments. In exchange for funding for projects, investors receive tax credits and other tax benefits associated with ownership of the project, such as losses and depreciation. Credits are claimed over a ten year period. The other tax benefits remain available as long as the ownership structure continues. These tax benefits, plus the possibility of cash proceeds from the eventual sale of the project, represent the investors' return on investment. The detail of the calculation of the Tax Credit amount is discussed in the later sections of this report.

According to IRC §42, the state agencies are responsible for determining which housing projects should receive tax credits and the dollar amount of tax credit allocated to each project. It also states that the state agencies must develop a Qualified Allocation Plan (QAP) that is approved by their governing body, and to be used for scoring and approval of each project during application and allocation process.

IRS requires the allocating agency to review the amount of Tax Credit at three points in time; application, allocation, and placed in service. For the purpose of this audit we reviewed the last phase of this process, which is also known as Construction Cost Certification process.

Asset Management division is responsible for the Construction Cost Certification function of the Low Income Housing Tax Credit (LIHTC) program at TDHCA. This includes oversight of properties and developers performances to ensure their compliance with objectives of TDHCA, as well as applicable rules and regulations set by IRS and any program related statutes. Asset Management is also responsible for issuance of IRS form 8609 (the Tax Credit certificate to the developers). TDHCA issues IRS form 8610 which is an annual form submitted to IRS at the end of each year that includes all IRS 8609s that have been issued during that calendar year.

Tax Credit Allocation

As noted previously, the state agencies are responsible for selecting which housing projects should be awarded tax credit, and the dollar amount of tax credit allocated to each project. Tax credits are awarded to eligible participants to offset a portion of their federal tax liability in exchange for the production or preservation of affordable rental housing. Investors in qualified affordable multifamily residential developments can use the LIHTCs as a dollar-for-dollar reduction of their federal income tax liability. Tax credit certificates are non-refundable. There are two types of Tax Credits: Competitive (9%) and Non-Competitive (4%). The 9% LIHTCs are designed to provide a 70% subsidy for developing or rehabilitating low-income units, and is based on industry estimates, and 4% LIHTC is providing a 30% subsidy.

The amount of credit the taxpayer can claim each year is determined as follows:

- Eligible Basis x Applicable Fraction = Qualified Basis
- Qualified Basis x Applicable Percentage = Annual Credit Amount

Eligible Basis is the total allowable cost associated with the depreciable residential rental project, which could be up to 130% of the actual costs if the building is located in a high cost area. **Applicable Fraction** is the portion of the rental units that are qualified as low-income units, and is determined as the lesser of square footage or number of units. The rent of low-income units must be restricted and cannot exceed 30% of the income limit applicable to the building location. **Applicable Percentage** is the percentage of basis that over the ten-year credit period provides credit amount equal to the present value of either 70% or 30% of the qualified basis, depending on the characteristics of the housing¹.

As a result of the Housing Assistance Act of 2008 Congress amended IRC§42 to provide a temporary minimum applicable percentage of 9% for new buildings regardless of the prevailing interest rate. In 2015 US Congress voted to permanently set 9% as minimum rate for applicable percentage. However, the 4% credit rate remained variable based on AFR. Tax credit calculations are discussed further towards the end of this report

Tax Credit Allocation Carryover

A project that has been awarded a competitive 9% tax credit allocation must be completed and occupied in the year that the allocation is received. However, it is common for the projects not to be completed and placed in service within that time frame. Therefore the state agencies issue **Carryover Allocations** that extended the required placed-in-service date to the end of the second calendar year after the allocation was issued. In order for a project to qualify for the carryover allocation a development must incur at least 10% of its anticipated costs within the calendar year in which the allocation was received.

Independent Auditor's Report

After completing the project (which has different deadlines depending on whether it is a 4% or 9% Tax Credit Property) the developers submit a packet to TDHCA that includes a certified report by an Independent Auditor who has reviewed the developer's eligible costs and financial records. This is known as Construction Cost Certification. Asset Management is responsible for reviewing the Construction Cost Certification packet and making recommendations to the Department's Executive Director for final approval of Tax Credit certificate.

The Construction Cost Certification is submitted to TDHCA in PDF and also Excel format for further review by Asset Management team. TDHCA has some built-in controls in the Excel spreadsheet formulas, such as maximum percentage of contractor's fees and developer's fees, to ensure that certain fees and costs are within TDHCA and underwriting rules. However, TDHCA doesn't seem to have any direct guidance in regard to selection of the CPA firm that performs the independent audit, nor does it provide instructions as to the process of the audit. The developers and CPA firms are instructed to refer to and follow IRS§42.

We reviewed and tested a sample of ten "Independent Auditor's report" and "Market Analysis" for each of the last three years. We found that in some cases the CPA firm that performed and provided the independent auditor's report was not licensed in the state of Texas. We also noted that in one instance the same entity provided both market analysis and the independent auditor's report for a project.

¹ 70% of the qualified basis of a new building that is not federally subsidized for the taxable year, and 30% of the qualified basis of all other buildings.

Issuance of IRS forms (8609 & 8610)

IRC §42 requires state agencies to submit annual reports to the IRS identifying the annual credit amount allocated to each building and project for the year, sufficient information to identify each building and the developer of each project, and other information needed for the administration of the program. The annual report is made by submitting IRS Form 8610, annual Low-Income Housing Credit Agencies Report, along with copies of the IRS Forms 8609 issued that year and Schedule A (Form 8610), and documenting credit carryover allocations, to the IRS by February 28th of the following year.

A copy of the signed IRS form 8609 for each building is forwarded to Multifamily Finance division (MF) at TDHCA, and the original is sent to the developer. Each year TDHCA prepares a Form 8610 for the IRS. This form reports all of the tax credits that were awarded for the year, which will be carried forward for ten years. The time between the award and the issuance of form 8609, the actual tax credit, varies. IRS Form 8609 will not be issued until the owner has provided evidence that all buildings have been placed in service by December 31st of the year the Commitment was issued or December 31st of the second year following the year the Carryover Allocation agreement was executed. TDHCA does not track the forms 8609 after that point.

Results

Our review of Asset Managements' procedures indicates that appropriate processes are in place for the Construction Cost certification function. We recommend that management establish procedures to ensure that the CPAs utilized by developers are in good standing with the Texas State Board of Public Accountancy (TSBPA).

Finding Item Number	Status Pertaining to the Recommendations and Action to be Taken	Target Completion Date	Responsible Party
19-004.01	OIA recommends that Asset Management require developers to verify CPA firm's licenses validity, including any restrictions, before hiring the firm to perform the audit	8/30/19	Rosalio Banuelos

Management response:

Finding Item Number 19-004.01 – Asset Management will implement the recommendation from OIA to require developers to verify CPA firm's licenses validity, including any restrictions.

Observation:

OIA Recommends that management consider establishing rules where the marketing Analysis and the CPA firm performing construction cost certification are not the same entity. Management agreed to evaluate the process further and discuss the recommendation with other divisions of the Department to determine if a change to the rules is warranted.

Tax Credit Computation

In this section we discuss computation methodology for calculating the tax credit allocations. The IRS prescribes from Section 42:

"Internal Revenue Code

§42. Low-income housing credit

(a) In general

For purposes of section 38, the amount of the low-income housing credit determined under this section for any taxable year in the credit period shall be an amount equal to-

- (1) the applicable percentage of*
- (2) the qualified basis of each qualified low-income building.*

(b) Applicable percentage: 70 percent present value credit for certain new buildings; 30 percent present value credit for certain other buildings

(1) Determination of applicable percentage

For purposes of this section-

(A) In general

The term "applicable percentage" means, with respect to any building, the appropriate percentage prescribed by the Secretary for the earlier of-

- (i) the month in which such building is placed in service, or*
- (ii) at the election of the taxpayer-*

(I) the month in which the taxpayer and the housing credit agency enter into an agreement with respect to such building (which is binding on such agency, the taxpayer, and all successors in interest) as to the housing credit dollar amount to be allocated to such building, or

(II) in the case of any building to which subsection (h)(4)(B) applies, the month in which the tax-exempt obligations are issued.

A month may be elected under clause (ii) only if the election is made not later than the 5th day after the close of such month. Such an election, once made, shall be irrevocable.

(B) Method of prescribing percentages

The percentages prescribed by the Secretary for any month shall be percentages which will yield over a 10-year period amounts of credit under subsection (a) which have a present value equal to-

- (i) 70 percent of the qualified basis of a new building which is not federally subsidized for the taxable year, and*
- (ii) 30 percent of the qualified basis of a building not described in clause (i).*

(C) Method of discounting

The present value under subparagraph (B) shall be determined-

- (i) as of the last day of the 1st year of the 10-year period referred to in subparagraph (B),*
- (ii) by using a discount rate equal to 72 percent of the average of the annual Federal mid-term rate and the annual Federal long-term rate applicable under section 1274(d)(1) to the month applicable under clause (i) or (ii) of subparagraph (A) and compounded annually, and*
- (iii) by assuming that the credit allowable under this section for any year is received on the last day of such year.*

(2) Minimum credit rate for non-federally subsidized new buildings

In the case of any new building-

(A) which is placed in service by the taxpayer after the date of the enactment of this paragraph, and (B) which is not federally subsidized for the taxable year, the applicable percentage shall not be less than 9 percent.”

The IRS program referred to as the “9%” tax credit program originally prescribed computing an amount of tax credits that would yield 70% of the qualified basis. The term 9% refers to an annual tax credit amount expressed as a percentage of the qualified basis. During the American Recovery and ReInvestment Act of 2008, a floor of 9% was set for the tax credit rate. This 9% floor was made permanent in 2015.

Based on our calculations, a 9% credit rate will yield 70% of the basis or greater until the applicable federal interest rate (or discount rate) rises to 7%. At that point, a tax credit rate of over 9% would be necessary to remain in compliance with Section 42.

The second tax credit scenario is the “4%” rate. For these noncompetitive tax credit deals, (where the tax credits pay for 30% of the qualified basis) the IRS calculates the “4%” tax credit rate on a monthly basis. The current tax credit rate is 3.25%.

Low-Income Housing Tax Credit Rates

The Internal Revenue Service each month publishes the credit percentages that apply to low-income housing tax credit buildings that are placed in service that month. There are two separate rates — one for 70% present value credit (PVC) and one for the 30% present value credit. NOTE: the 70% rate is currently fixed by statute at a floor of 9%. The 70% rate is available for low-income new construction and substantial rehabilitation expenditures that aren’t federally subsidized (e.g.; funded with tax-exempt bond proceeds or with below market federal loans).

The maximum 30% rate applies to acquisition expenditures and to federally subsidized low-income new construction or substantial rehabilitation expenditures for low-income buildings.

<i>LIHTC Rates²</i>	<i>70% PVC</i>	<i>30% PVC</i>
<i>June 2019</i>	<i>7.59</i>	<i>3.25</i>
<i>May 2019</i>	<i>7.59</i>	<i>3.25</i>
<i>April 2019</i>	<i>7.63</i>	<i>3.27</i>
<i>March 2019</i>	<i>7.63</i>	<i>3.27</i>
<i>February 2019</i>	<i>7.64</i>	<i>3.27</i>
<i>January 2019</i>	<i>7.70</i>	<i>3.30</i>

² The monthly LIHTC rate are published by www.housingonline.com/resources/facts-figures/low-income-housing-tax-credit-rates

We performed re-computations of applicable tax credit rates and tax credit amounts. Based on our test sample, the computations of tax credits were accurate.

OIA extends our sincere appreciation to management and staff of the Asset Management Division for their cooperation and assistance during the course of this audit.

Sincerely,

A handwritten signature in black ink that reads "Mark Scott". The signature is written in a cursive, flowing style.

Mark Scott, CPA, CIA, CISA, CFE, MBA
Internal Audit Director

MS/NS, CK

Report Item

2

AUDIT AND FINANCE COMMITTEE ACTION REQUEST

INTERNAL AUDIT DIVISION

June 27, 2019

Report on the status of the external audit activities

Report Item

Verbal Report