

Federal Housing Finance Agency
Office of Inspector General



FHFA Complied with Applicable Improper Payment Requirements During Fiscal Year 2014

Audit Report • AUD-2015-001 • May 14, 2015



AUD-2015-001

May 14, 2015

Executive Summary

Why OIG Did This Report

OIG is required by the Improper Payments Information Act of 2002 (IPIA), as amended by the Improper Payments Elimination and Recovery Act of 2010 (IPERA) and the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA) (collectively, “IPIA, as amended”), to determine annually whether the Federal Housing Finance Agency (FHFA) complied with the IPIA, as amended, during the prior fiscal year. OIG is further required to submit a report regarding such compliance to the head of FHFA, Congressional oversight committees, the Comptroller General of the United States, and the controller of Office of Management and Budget (OMB). OIG conducted a performance audit to assess FHFA’s compliance with the IPIA, as amended, for fiscal year 2014.

What OIG Found

OIG concluded that FHFA complied with the applicable provisions of the IPIA, as amended, as well as related criteria established in OMB Memorandum M-15-02. FHFA has opined that not all provisions of the IPIA, as amended, are applicable because they apply to federal funds, and FHFA does not finance its operations with federal funds.

OIG, however, recognizes that FHFA is acting to achieve the intent of the IPIA, as amended, and the related OMB Memorandum M-15-02, regardless of its determination that it is not required to do so.

This audit was led by Jude Koval, Audit Manager, who was assisted by Jacob Trewe, Senior Auditor, and Darryl Stephens, Senior Writer/Editor. We appreciate the cooperation of FHFA staff, as well as the assistance of all those who contributed to the preparation of this report.

This report has been distributed to the Congress, OMB, and others and will be posted on OIG’s website, www.fhfaoig.gov.

Heath Wolfe
Assistant Inspector General for Statutory Audits
Office of Audits

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ABBREVIATIONS

AFR	Annual Financial Report
FHFA	Federal Housing Finance Agency
IPERA	Improper Payments Elimination and Recovery Act of 2010
IPERIA	Improper Payments Elimination and Recovery Improvement Act of 2012
IPIA	Improper Payments Information Act of 2002
OGC	Federal Housing Finance Agency, Office of General Counsel
OIG	Federal Housing Finance Agency, Office of Inspector General
OMB	Office of Management and Budget
PAR	Performance Accountability Report
U.S.C.	United States Code

CONTEXT

Definition of Improper Payment

Federal agencies regularly make payments to program beneficiaries, grantees, vendors, and contractors, or on behalf of program beneficiaries. Some of these payments may be “improper” in one or more respects. For example, they may be made to the wrong recipients in the wrong amounts, at the wrong times, or for the wrong reasons. OMB defines an improper payment as:

An improper payment is any payment that should not have been made or that was made in an incorrect amount under statutory, contractual, administrative, or other legally applicable requirements. Incorrect amounts are overpayments or underpayments that are made to eligible recipients (including inappropriate denials of payment or service, any payment that does not account for credit for applicable discounts, [footnote omitted] payments that are for an incorrect amount, and duplicate payments). An improper payment also includes any payment that was made to an ineligible recipient or for an ineligible good or service, or payments for goods or services not received (except for such payments authorized by law). In addition, when an agency’s review is unable to discern whether a payment was proper as a result of insufficient or lack of documentation, this payment must also be considered an improper payment.¹

Legislative Controls to Prevent and Detect Improper Payments

IPIA was enacted on November 26, 2002, to provide for estimates and reports of improper payments by federal agencies.² IPIA was amended by IPERA on July 22, 2010, to help prevent the further loss of billions in taxpayer dollars.³ IPIA, as amended by IPERA, requires federal agencies to periodically review, determine, estimate, and report programs and activities that may be susceptible to significant improper payments. IPERIA, enacted on

¹ OMB Memorandum M-15-02, Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments* (October 20, 2014) [hereinafter OMB Memo M-15-02, App. C], Part I ¶¶ 2 and 3. OMB Circular A-123, *Management’s Responsibility for Internal Control* (December 31, 2004), provides guidance to federal agencies on improving the accountability and effectiveness of federal programs and operations by establishing, assessing, correcting, and reporting on internal control.

² Public Law No. 107-300, 31 U.S.C. § 3321 note.

³ Public Law No. 111-204, 31 U.S.C. § 3321 note.

January 10, 2013, further amended IPIA and IPERA to intensify efforts to identify, prevent, and recover payment error, waste, fraud, and abuse within federal spending.⁴

IPIA, as amended, defines the term “payment” as:

[A]ny transfer or commitment for future transfer of Federal funds such as cash, securities, loans, loan guarantees, and insurance subsidies to any non-Federal person or entity or a Federal employee, that is made by a Federal agency, a Federal contractor, a Federal grantee, or a governmental or other organization administering a Federal program or activity.⁵

Requirements Under IPIA, as Amended

Pursuant to the requirements in the IPIA, as amended, federal agencies should intensify efforts to eliminate payment errors, waste, fraud, and abuse, including reducing and recapturing erroneous payments.

In accordance with OMB Memorandum M-15-02—which implements the requirements of the IPIA, as amended—agencies must follow a four-step process:

Step 1: Review all programs and activities and identify those that are susceptible to significant improper payments.

Step 2: Obtain a statistically valid estimate of the annual amount of improper payments in programs and activities that are identified in Step 1.

Step 3: Implement a plan to reduce improper payments.

Step 4: Report annually on improper payments in a performance accountability report (PAR) or annual financial report (AFR).^{6, 7}

Additionally, to comply with the IPIA, as amended, each fiscal year, Inspectors General are required to review their establishments’ improper payment reporting in their annual PARs or AFRs to determine whether they are in compliance with the IPIA, as amended, and to report

⁴ Public Law No. 112-248, 31 U.S.C. § 3321 note.

⁵ Public Law No. 111-204, 31 U.S.C. § 3321 note; see also OMB Memorandum M-15-02, Appendix C, *supra* note 1, at Part I ¶¶ 2 and 3.

⁶ OMB Memo M-15-02, App. C, *supra* note 1, at Part I ¶ 9.

⁷ A PAR provides both financial and performance information that enables the President, the Congress, and the public to assess the performance of an agency relative to its mission and to demonstrate accountability. An AFR provides similar information, but excludes performance information. See OMB Circular A-136 p. 10 (revised, October 21, 2013).

their findings.⁸ Inspectors General are expected to complete their reviews and determinations within 180 days after their establishments' publication of their PARs or AFRs.⁹ In addition, as part of his/her review, an Inspector General should confirm that the establishment has:

- a. Published an AFR or PAR for the most recent fiscal year and posted that report and any accompanying materials required by OMB on the agency website;
- b. Conducted a program specific risk assessment for each program or activity that conforms with Section 3321 note of Title 31 U.S.C. [i.e., IPIA, as amended] (if required);
- c. Published improper payment estimates for all programs and activities identified as susceptible to significant improper payments under its risk assessment (if required);
- d. Published programmatic corrective action plans in the AFR or PAR (if required);
- e. Published, and is meeting[footnote deleted], annual reduction targets for each program assessed to be at risk and estimated for improper payments (if required and applicable); and
- f. Reported a gross improper payment rate of less than 10 percent for each program and activity for which an improper payment estimate was obtained and published in the AFR or PAR.¹⁰

In the event it is determined that an agency does not meet one or more of the requirements, then the agency is not compliant with the IPIA, as amended. Agencies determined to be noncompliant are required to submit a plan to the Congress describing the actions the agency will take to come into compliance.¹¹ Further, OMB will notify agencies of additional required actions as needed based on the compliance level of each agency. OMB Memorandum M-15-02 provides detailed information on agency compliance planning and related efforts to become compliant.

⁸ IPERA § 3(b), *see* 31 U.S.C. § 3321 note.

⁹ OMB Memo M-15-02, App. C, *supra* note 1, at Part II § A(2). FHFA issued its PAR on November 17, 2014, so the 180-day deadline falls on May 15, 2015.

¹⁰ OMB Memo M-15-02, App. C, *supra* note 1, at Part II § A(3).

¹¹ IPERA § 3(c)(1)(A), *see* 31 U.S.C. § 3321 note.

FHFA Has Determined that Not All Requirements Under IPIA, as Amended, Are Applicable to FHFA

In its fiscal year 2014 PAR, dated November 17, 2014, FHFA states that:

IPIA requires that agencies: (1) review activities susceptible to significant erroneous payments; (2) estimate the amount of annual erroneous payments; (3) implement a plan to reduce erroneous payments; and (4) report the estimated amount of erroneous payments and the progress to reduce them. IPIA defines significant erroneous payments as the greater of 2.5% of program activities and \$10 million.

FHFA, in the spirit of compliance and as part of a sound internal control structure, has established controls to detect and prevent improper vendor payments. FHFA has identified no activities susceptible to significant erroneous payments that meet IPIA's thresholds. Additionally, FHFA pursues the recovery of all improper payments.¹²

Although FHFA states that it has established controls to detect and prevent improper payments in the spirit of the IPIA, as amended, FHFA maintains that most requirements of the IPIA, as amended, and guidance such as OMB Memorandum M-15-02, are not applicable to FHFA.¹³ Table 1 summarizes the requirements of the IPIA, as amended, and OMB Memorandum M-15-02 that FHFA considers inapplicable to its operations.

¹² Page 105 of FHFA's fiscal year 2014 PAR cited actions regarding erroneous payments.

¹³ FHFA, *Associate General Counsel Memorandum*, originally dated February 7, 2012, updated February 15, 2012, and subsequently reconfirmed on December 16, 2013, and January 8, 2015.

TABLE 1. FHFA’S COMPLIANCE UNDER IPIA, AS AMENDED, FOR FISCAL YEAR 2014

Compliance Element	FHFA Action
The agency has published an annual PAR or AFR for the most recent fiscal year and posted that report and any accompanying materials required under guidance of OMB on the agency website.	FHFA published its 2014 PAR and included relevant information pertaining to improper payments.
The agency has conducted a program specific risk assessment for each program or activity that conforms with the IPIA, as amended (31 U.S.C. § 3321 note) (if required).	FHFA determined that this section of the IPIA, as amended, is not applicable.
The agency has published improper payments estimates for programs and activities identified as susceptible to significant improper payments under its risk assessment (if required).	FHFA determined that this section of the IPIA, as amended, is not applicable.
The agency has published programmatic corrective action plans in its PAR or AFR (if required).	FHFA determined that this section of the IPIA, as amended, is not applicable.
The agency has published, and is meeting, improper payments reduction targets for each program assessed to be at risk and estimated for improper payments (if required and applicable).	FHFA determined that this section of the IPIA, as amended, is not applicable.
The agency has reported a gross improper payment rate of less than 10% for each program and activity for which an estimate was obtained and published in its PAR or AFR.	FHFA determined that this section of the IPIA, as amended, is not applicable.

FHFA’s Office of General Counsel (OGC) has concluded that various subsections of the IPIA, as amended, are only applicable to payments made with federal funds, and that FHFA funds are not to be construed as government or public funds.¹⁴ Hence, OGC reasons that the payments FHFA makes, such as payments to vendors, are not transfers of federal funds.¹⁵ Further, because FHFA does not make payments with federal funds, OGC concludes that FHFA is not required to conduct program specific risk assessments even if the payments FHFA makes fall within the specified dollar thresholds that trigger program assessments.¹⁶ Finally, OGC contends that actions to achieve compliance with the IPIA, as amended (e.g., Congressionally directed reprogramming, transfer, and reauthorization of programs and

¹⁴ *Id.*, citing 12 U.S.C. § 4516(f).

¹⁵ *Id.*

¹⁶ *Id.*

activities), are not actions that are available to FHFA in light of its status as an independent regulatory agency that does not seek appropriations for its activities.¹⁷

OIG's Office of the Chief Counsel assessed whether OGC's analysis of the applicable legal authorities is reasonable. Upon due consideration of that analysis and the authorities in question, it determined that OGC's analysis is reasonable, so OIG does not contest the OGC conclusions referenced above.

FHFA's Internal Controls over Financial Reporting

With respect to FHFA following the spirit of the IPIA, as amended, FHFA reports that it has established and maintains internal controls over payments to detect and prevent improper payments made to vendors.¹⁸ FHFA provided OIG with relevant vendor invoice and payment desktop procedures that FHFA implemented to ensure that a system of internal controls is followed to mitigate the potential for fraud, misuse, and payment delinquency. OIG reviewed the procedures and noted no design flaws within the control.

Additionally, GAO annually reviews and provides an opinion on the effectiveness of FHFA's internal controls over financial reporting. GAO assesses, evaluates, and determines whether such internal controls are properly designed and operating effectively in all material respects.¹⁹ In its *Financial Audit: Federal Housing Finance Agency's Fiscal Years 2014 and 2013 Financial Statements* report, GAO identified deficiencies in FHFA's internal controls over financial reporting (that GAO did not consider to be a material weakness or significant deficiency).²⁰ However, GAO did not identify any issues related to the design and effectiveness of FHFA's vendor invoice and payment process control, and there were no findings relating to the accuracy of disbursements.

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ GAO's audit was not designed to express an opinion on the effectiveness of FHFA's internal controls related to improper payments or FHFA's compliance with the IPIA, as amended, specifically, but rather it was intended to assess controls over financial reporting generally. Consequently, GAO's audit may not identify all deficiencies in FHFA's internal controls over financial reporting that are less severe than a material weakness. According to the American Institute of Certified Professional Accountants' *Professional Standards*, AU-C § 265.07, a deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis.

²⁰ *Id.* A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

CONCLUSIONS

OIG concludes that FHFA complied with the annual PAR or AFR reporting requirement of the IPIA, as amended. As to the remaining requirements, FHFA opined that they are not applicable, and OIG does not contest FHFA's interpretation.

Nonetheless, OIG recognizes that FHFA is acting to achieve the intent of the IPIA, as amended, and the related OMB Memorandum M-15-02, regardless of its determination that it is not required to do so. Specifically, in the spirit of compliance and as part of a sound internal control structure, FHFA has established controls to detect and prevent improper vendor payments. For example, FHFA's invoice payment processing procedures include detailed instructions on properly verifying the accuracy of vendor invoice amounts prior to payment.

OBJECTIVE, SCOPE, AND METHODOLOGY

Objective

OIG’s audit objective was to determine whether FHFA is in compliance with the IPIA, as amended, as well as criteria established in OMB Memorandum M-15-02.

Scope

This audit covered FHFA’s efforts to comply with the IPIA, as amended, and OMB Memorandum M-15-02 requirements to detect, prevent, and report improper payments during FHFA’s fiscal year period October 1, 2013, to September 30, 2014. To accomplish the audit objective, OIG reviewed applicable statutes, executive orders, and other related compliance requirements on improper payments; reviewed various GAO audit reports; met with key FHFA officials; obtained sufficient and appropriate evidence on compliance actions taken (e.g., confirmed that FHFA’s 2014 PAR was posted to its website and reviewed OGC correspondence); and reviewed and assessed improper payment element requirements and related activities. OIG conducted its field work during December 2014 through February 2015 and issued its report in accordance with OMB requirements (i.e., within 180 days of publication of FHFA’s PAR).

Methodology

OIG’s review of FHFA’s internal controls designed to comply with the IPIA, as amended, requirements was limited. OIG reviewed FHFA’s written documentation and legal opinions related to its determination that the IPIA, as amended, provisions—and therefore most improper payment compliance elements—are not applicable to FHFA. OIG also reviewed IPERIA to ascertain whether FHFA is subject to the Act’s requirements. FHFA determined that IPERIA—like IPIA and IPERA—do not apply to FHFA because it does not utilize appropriated funds. For this reason, the funds used by FHFA to make payments do not qualify as federal funds under applicable law, and therefore most of the various improper payments requirements set forth by these statutes are not triggered. OIG confirmed the posting of the 2014 PAR and accompanying materials on FHFA’s external website in accordance with OMB guidance and the inclusion of appropriate language that FHFA established and maintains internal control procedures for handling improper payments.

OIG conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that audits be planned and performed to obtain sufficient, appropriate evidence to provide a reasonable basis for OIG’s findings and

conclusions based on the audit objective. OIG believes that the evidence obtained provides a reasonable basis for the conclusions included herein, based on the audit objective.

APPENDIX A


FHFA's Comments



Federal Housing Finance Agency

MEMORANDUM

TO: Bryan Saddler
Acting Deputy Inspector General for Audits

FROM: Mark Kinsey 
Chief Financial Officer

SUBJECT: Audit Report: *FHFA Complied with Applicable Improper Payment Requirements during Fiscal Year 2014*

DATE: May 6, 2015

Thank you for the opportunity to respond to the Federal Housing Finance Agency Office of Inspector General's (OIG) draft audit report titled, *FHFA Complied with Applicable Improper Payment Requirements During Fiscal Year 2014* (Report). The Report presents the results of the OIG's performance audit to assess Federal Housing Finance Agency's (FHFA) compliance with the Improper Payments Information Act of 2002 (IPIA), as amended.

I am pleased that the OIG concluded that FHFA complied with the applicable provisions of the IPIA, as amended, as well as criteria established in the OMB Memorandum M-15-02. The Report recognized that in the spirit of compliance and as part of a sound internal control process, FHFA had established controls to detect and prevent improper vendor payments and FHFA's invoice payment processing procedures include detailed instructions on properly verifying the accuracy of vendor invoice amounts prior to payment.

I would like to acknowledge the dedicated OIG staff that worked with FHFA during this audit.

If you have any questions relating to our response, please do not hesitate to call me at (202)649-3780.

ADDITIONAL INFORMATION AND COPIES.....

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Attn: Office of Investigation – Hotline
400 Seventh Street, S.W.
Washington, DC 20024