

Executive Summary

The 2016 audited financial statements of OHCS outline assets in excess of liabilities of \$221 million however that “net position” can only be utilized after bond indenture reserve requirements are funded. A spreadsheet outlining those reserve requirements is included at the bottom of this appendix document, and ultimately demonstrates unrestricted cash and investments of about \$35 million. OHCS contracts with an independent financial advisor to determine how much of that unrestricted cash is available for distribution to pay for general program oversight and agency operations. That amount is currently capped at \$6.1 million/year. For future years, increased availability of distributions will be driven by the agency’s ability to have a larger, more liquid balance sheet. Unfortunately until interest rates normalize and other market conditions become favorable for its products, OHCS is in a situation where the balance sheet is shrinking. Since 2013 OHCS has averaged \$45 million more in payoffs than loan originations each year. This is a large factor that has led to a decline in assets of about \$322M or nearly 21% of its balance sheet in that same time period. OHCS is not in danger of a fiscal problem however is constrained by the reserve requirements of the bond indentures.

OHCS BOND INDENTURE DISTRIBUTIONS SUMMARY

Mortgage Revenue Bonds (Single-Family Mortgage Program) (“MRB”)

Current Annual Distributions

Based on the most recent Cash Flows Projections (July 1, 2015 basis), \$4,300,000 of distributions are estimated to be available on or after July 1 of each year. However, based on the factors described below and various assumptions that Moody’s requires to be modeled into the Cash Flow Projections for this Indenture to maintain an Aa2 bond rating, the current cash flows can only sustain \$4,300,000 of annual distributions **through 2021**.

Indenture Requirements for Distributions

Distributions for single-family program expenses to the extent that Cash Flow Projections demonstrate an Asset-to-Liability ratio of 100% after the distribution has occurred; distributions for other purpose (“free and clear”) to the extent that Cash Flow Projections demonstrate an Asset-to-Liability ratio of 102% after the distribution has occurred.

Factors That Impact Future Distribution Amounts

Decreasing Loan Portfolio - Since 2008, this indenture has seen a steady and significant decrease in the amount of outstanding Mortgage Loans. Historically low mortgage rates have resulted in both

significant increases in the prepayment speed of existing loans and decreases in new loan origination resulting from competition from other mortgage products. Reduced affordability in areas of Oregon where most OHCS single-family loan activity occurs has also contributed to this decline. If the current trend continues, OHCS's ability to take \$4,300,000 of annual distributions could be impacted.

Risk of Future Loan Losses – Since 2008, significant losses resulting from delinquencies and foreclosures occurred in this indenture. While these losses appear to have finally stabilized, if another decline in the housing market in Oregon were to occur, particularly with such dramatic recent increases in housing prices in certain areas of the State, this indenture could again begin experiencing significant losses. With changes to the FHA requirements for mortgage insurance, we now have a larger percentage of uninsured mortgage loans in our portfolio, as borrowers are now using secondary financing to get our first-lien loans at or below the 80% loan-to-value ratio that allows these to be financed under the indenture without mortgage insurance. In the event of another major decline in the housing, this higher number of uninsured loans could possibly increase future losses. Therefore, these factors could have a significant impact on future distributions by reducing the amount of annual distributions available for normal program administrative costs.

Changes in Rating Agencies Cash Flow Assumptions - Moody's requires various assumptions be modeled into the Cash Flow Projections for each bond program. Often times these assumptions are extreme and intended to demonstrate that bond indentures are able to withstand high degrees of stress and still remain financial sound. For single-family bond programs, changes to ratings assumptions related to loss exposure based on mortgage insurance, type of loans, investment rates and prepayment speeds can have a significant impact on the amount of bond distributions that can be taken from the indenture; future tightening of these Cash Flow assumptions could impact OHCS's ability to take \$4,300,000 of annual distributions.

Risk of Negative Arbitrage – The MRB indenture has many unique risks that currently don't exist in our other bond indentures. This indenture is currently the only one that we are actively originating loans, so negative arbitrage that results from very low investment rates continues to put stress on these Cash Flows.

Interest Rate Risk and Interest Rate Swaps – Approximately 38% of the outstanding bonds in the indenture are variable rate of which about 71% are currently hedged. The unhedged variable bonds are subject to interest rate risk when rates rise and all variable rate bonds are subject to risks related to failed weekly remarketings. Even with the hedges that OHCS uses to mitigate interest rate risk on variable rate debt, there are still certain risks related to swap transactions including counterparty risk, amortization risk, and housing sector risk; OHCS also needs to have reserves available in the event that collateralization requirements in these swap agreements are to be triggered.

Liquidity Provider Risk – OHCS uses highly rated banks to provide liquidity for its variable rate debt under standby bond purchase agreements. The credit quality of the liquidity provider impacts the variable rate resets on the bonds. If the investors in OHCS variable rate debt lose faith in the credit

quality of one of OHCS's liquidity providers, the cost of such debt could increase significantly until an alternative provider or financial structure can be achieved.

Indenture Risk Mitigation – As discussed above, OHCS has used a variety of financial structures that involve certain risks in order to continue to operate its program of providing affordable single family housing and generating revenue to fund other Department programs. OHCS prudently manages these risks through a variety of strategies. However, a significant component of each risk mitigation strategy includes the availability of excess reserves available under the indentures to provide options under difficult market conditions.

Continuation of the Program – OHCS continues to operate its program by periodically issuing new bonds and using the proceeds to purchase newly originated mortgage loans. Issuing bonds requires an investment of indenture resources to pay the cost of issuance. The bond issue then generates revenue over time that can be used to cover such costs. Funds must continue to be available to pay cost of issuance in order for the program to continue.

Current MRB Rating and Impact of Future Ratings Downgrade

Currently, Moody's has assigned the following ratings to bonds issued under the MRB Indenture: Aa2 with stable outlook (long-term bonds) and Aa2/VMIG 1 with stable outlook (short-term bonds). As the only parity bond indenture that OHCS is currently issuing debt under, any future downgrade to these ratings would have a significant impact to the single-family mortgage program.

If the MRB ratings were to be downgraded by one step to Aa3, the cost of borrowing could increase by as much 15 basis points initially, stabilizing back to around a 10 basis point increase over the long-term. With current rate compression between tax-exempt and taxable interest rates, such increases in the cost of borrowing could severely impact OHCS ability to offer below-market mortgage rates to borrowers while remaining profitable. Even with the current MRB ratings in today's market, OHCS already has to use complex bond structures and leverage existing resources in the MRB indenture to be able to offer below-market rate mortgage rates to program borrowers. A 10-15 basis point increase in the cost of borrowing would significantly decrease OHCS's capacity to finance program loans as the additional resources in the MRB indenture needed to complement our bond structure would be stretched considerably thinner.

If MRB ratings were to be downgraded by more than one step (that is to A1 or less), it's likely the single-family mortgage program would no longer be viable. Currently, an indenture rating of Aa3 is considered to be an investor threshold for single-family mortgage programs, especially as many state housing finance agencies have migrated their single-family bond programs to Mortgage-Backed Securities structures which have Aaa ratings. At present, there are no state housing finance agencies that have active single-family bond programs with ratings of A1 or less.

A downgrade to the MRB ratings would also have other negative impacts to the indenture. One of OHCS's current bond liquidity agreements (required for all variable rate bonds) contains a downgrade provision that would trigger fee increases ranging from approximately 27% - 372% depending on the severity of the downgrade; OHCS's other bond liquidity agreement includes a fee escalator provision of approximately 45% if the MRB indenture Asset-to-Liability ratio were to decline to certain thresholds when distributions have been used for purposes other than administrative expenses of the variable rate bonds. A downgrade to the MRB ratings would also likely require OHCS to post collateral pursuant to the various swap agreements that hedge variable rate debt in the MRB indenture.

Housing Revenue Bonds (Single-Family Mortgage Program) ("HRB")

Current Annual Distributions

Based on the most recent Cash Flows Projections (July 1, 2015 basis), no distributions are currently projected in this indenture. To date, no distributions have been taken from this Indenture. The HRB indenture is a relatively new bond indenture having only been created in December 2009. As is typical with most new bond indentures, this indenture is expected to take several more years to season; until that time, no future distributions are anticipated to be available from this indenture.

Indenture Requirements for Distributions

Because this indenture was used to issue bonds between 2009 and 2012 under the federal government's New Issue Bond Program ("NIBP"), pursuant to the NIBP Agreement between OHCS and U.S. Treasury, all distributions from this indenture are subject to U.S. Treasury approval.

Factors That Impact Future Distribution Amounts

Decreasing Loan Portfolio - This indenture was created specifically to issue bond under NIBP; since this program expired at the end of 2012, no additional bond issuance has subsequently occurred and the last proceeds used to purchase loans were expended in 2014. Historically low mortgage rates have resulted in significant amounts of prepayments even for these newer mortgage loans originated since 2011. Of the original 1,428 loans finance from this indenture, only 967 remained outstanding as of October 1, 2016.

Risk of Future Losses – Since this indenture is still relatively new, delinquencies and foreclosures have only recently started to normalize. Changes in recent years to the FHA requirements for mortgage insurance have resulted in a higher percentage of uninsured mortgage loans in this portfolio, as borrowers are now using secondary financing to get our first-lien loans at or below the 80% loan-to-value ratio that allows these to be financed under the indenture without mortgage insurance. In the event of another major decline in the housing, this higher number of uninsured loans could possibly increase future losses.

Changes in Rating Agencies Cash Flow Assumptions - Moody's requires various assumptions be modeled into the Cash Flow Projections for each bond program. Often times these assumptions are extreme and intended to demonstrate that bond indentures are able withstand high degrees of stress and still remain financial sound. For single-family bond programs, changes to ratings assumptions related to loss exposure based on mortgage insurance, type of loans, investment rates and prepayment speeds can have a significant impact on the amount of bond distributions that could be taken in future periods from the indenture.

Multifamily Housing Revenue Bonds ("MF")

Current Annual Distributions

Based on the most recent Cash Flows Projections (July 1, 2015 basis), \$1,750,000 of distributions are estimated to be available on or after July 1 of each year. However, based on the factors described below and various assumptions that Moody's requires to be modeled into the Cash Flow Projections for this Indenture to maintain an Aaa (stable) rating, the current cash flows can only sustain \$1,750,000 of annual distributions **through 2050**.

Indenture Requirements for Distributions

Distributions for any purpose ("free and clear") to the extent that Cash Flow Projections demonstrate the availability of assets after debt service payments have been made and all indenture required reserves have been funded.

Factors That Impact Future Distribution Amounts

Decreasing Loan Portfolio - This indenture was created to finance multifamily mortgage loans insured by the FHA Risk Sharing program and other permitted credit enhancements. To date, this indenture has been used exclusively to finance FHA Risk Sharing insured loans. Currently, no new mortgage loans are being financed from this indenture (the last such financing occurring in 2012). In addition, several of the loans financed from bonds issued under this indenture have either been prepaid or have requested the ability to prepay in the future. The current estimated annual distributions of \$1,750,000 are based on an assumption that only seven specific Risk Sharing loans in this indenture are assumed to prepay. Many of the loans in this portfolio were financed in the mid to late 1990's as acquisition/rehabilitation projects, most of which are now facing major capital improvement needs. As such, it is likely additional prepayment requests will be received and granted by OHCS going forward. These additional prepayments will reduce the amount of future annual distributions that will be able to be taken from this indenture.

Risk of Future Losses – Because many of the projects financed by this indenture have significant capital improvement needs, health and safety issues, high vacancy rates and continue to experience low Debt Coverage Ratios, there is a significant risk of potential future losses in this indenture. As the name suggests, the FHA Risk Sharing program results in any such losses being shared between HUD (the insurer) and OHCS (as mortgagor). If a loan defaults, HUD will make full payment under the insurance, and OHCS will be responsible for reimbursing HUD for OHCS's share (50%) of these payments. In order to provide assurance of OHCS's ability to repay HUD, other reserves (in addition to those required by the indenture) need to be available for such contingencies.

Other Indenture Risks – The MF indenture also has some other risks similar to the MRB indenture. Approximately 9% of the outstanding bonds in the indenture are variable rate, all of which are currently hedged. These variable rate bonds are subject to risks related to failed weekly remarketings. Even with the hedge that OHCS uses to mitigate this interest rate risk, there is still risk related to counterparties and the need for future collateral to support these transactions. While OHCS is prudently managing this risk, it is largely mitigated by having excess reserves available in the indenture.

Elderly and Disabled Housing Bonds (“E & D”)

Current Annual Distributions

Based on the most recent Cash Flows Projections (July 1, 2015 basis), \$4,300,000 of distributions are estimated to be available on or after August 1 of each year. However, based on the factors described below and various assumptions modeled into the Cash Flow Projections for this Indenture, the current cash flows can sustain \$1,500,000 of annual distributions through 2048.

Indenture Requirements for Distributions

Elderly and Disabled Housing Bonds are issued as State of Oregon General Obligation bonds pursuant to Article XI –I of the Oregon Constitution. As such, any available distributions from E & D (to the extent that Cash Flow Projections demonstrate the availability of assets after debt service payments have been made and all indenture required reserves have been funded) **are constitutionally restricted for purposes related to elderly and disabled housing**. As such, the E & D indenture only provides for “free and clear” distribution of these bonds once no E & D bonds remain outstanding (and the appropriate legal actions have been taken to release these constitutionally dedicated funds).

Factors That Impact Future Distribution Amounts

Decreasing Loan Portfolio - Currently, no new mortgage loans are being financed from this indenture (the last such financing occurring in 2007). Many of the loans financed from bonds issued under this indenture have either been prepaid or requested future prepayment or have either been modified with a reduced interest rate and /or an extend maturity date or requested such modification in the future.

Most of the loans in this portfolio were financed in between 1990 and 2003, and now have major capital improvement needs. OHCS is actively working to address each project's needs; therefore, it is likely additional prepayment and modifications requests will be received and granted by OHCS going forward. As the size of this loan portfolio decreases, so too will the amount of annual distributions that will be available from this indenture to be used for other purposes related to elderly and disabled housing.

Combined Program Account ("CPA")

History

This account was established in December 1980 as a general reserve to support the agency's various revenue bond programs. These funds are governed by a separate Indenture (similar to those created for bond programs) which provides certain protections as to the use of these funds. While no debt is issued pursuant to this Indenture, these funds have been available to support various bond programs throughout the agency's history. Currently, these funds are pledged to support debt service payments in the MRB indenture if needed and are considered when Moody's periodically confirms ratings for the MRB indenture. These funds are also currently pledged for any swap payments (including termination payments) that might become due under the MF indenture. In the past, these funds have also been pledged to support activities of the OHCS's Multiple Purpose Bonds and Housing Finance Revenue Bonds (Single-Family Mortgage Program) and to provide reserves a program collaboration with Fannie Mae. The CPA has also provided OHCS with temporary funds to finance multifamily mortgage loans that were eventually reimbursed from bond proceeds of bonds issued under the MF indenture. The funds held in the CPA also serve as the primary assets that support OHCS's "A2" Issuer rating from Moody's. Since the early 1990's, assets held in the CPA have been maintained and allowed to grow without having been expended.

Current OHCS Issuer Rating and Impact of Future Ratings Downgrade

Currently, Moody's has assigned OHCS an "Issuer Credit Rating" (or "ICR") of A2 with Stable outlook. The purpose of this rating is to provide investors an assessment of the relative financial strength of the agency based on available resources of the entity not directly restricted by bond indentures. This rating is often used to compare the financial strength of all state housing finance agencies; in fact, Moody's publishes a specific report that includes a listing of the Issuer ratings for all state housing finance agencies. In the past, OHCS used this rating to support the rating assigned to the Multiple Purpose Bond indenture. It has also used this rating to exempt itself from reserve requirements of the FHA Risk Sharing program. OHCS's ICR is also available to provide credit support for future OHCS bond programs and initiatives.

A downgrade to OHCS current agency/issuer rating of A2 would likely preclude OHCS from using that rating to support the credit of bond issues in future and from collaborating on housing programs with

other public or private entities. It would also likely require OHCS to post reserves amounts of as much as \$2,500,000 to be in compliance with requirement of the FHA Risk Sharing program. While not directly supporting any of OHCS's current bond indentures, any downgrade to OHCS Issuer rating would tarnish the agency's reputation among investors and would likely impact future borrowing costs as such downgrades are usually viewed by investors as a sign of general weakening of all bond program administered by the issuer and raise questions on the part of investors and rating agencies about the management of the issuer.

**OREGON HOUSING & COMMUNITY SERVICES DEPT
ANALYSIS OF CASH & INVESTMENTS - BY PROGRAM
AS OF JUNE 30, 2016**

	Housing Finance Fund								
	Housing Finance Account	Combined Program Account	Housing Revenue Bonds	Mortgage Revenue Bonds	Multi-Family Housing Revenue Bonds	Total Housing Finance Fund	Elderly & Disabled Housing Program	Total Enterprise Funds	
Cash & Cash Equivalents	9,652,837	267,112	7,946,661	43,997,905	2,043,148	63,907,663	25,289,122	89,196,785	
Investments (at Market Value)	967,497	18,406,434	12,015,243	219,406,677	24,883,120	275,678,971	2,945,873	278,624,844	
Total Cash & Investments	10,620,334	18,673,546	19,961,904	263,404,582	26,926,268	339,586,634	28,234,995	367,821,629	
Less: Amounts Held For Others									
Arbitrage Rebate Liability (for Fed. Govt.)	0	0	0	0	0	0	0	0	
Department FAF Account (for Borrowers)	(1,039,278)	0	0	0	0	(1,039,278)	0	(1,039,278)	
Unpaid Risk Sharing Premiums (for HUD)	0	0	0	0	(190,322)	(190,322)	0	(190,322)	
Oregon Rural Rehabilitation Funds (for Borrowers)	(850,728)	0	0	0	0	(850,728)	0	(850,728)	
Ready-to-Rent Commitment (for Local HFA's)	(273,389)	0	0	0	0	(273,389)	0	(273,389)	
Pre-Development Fund (for Borrowers)	(5,191,830)	0	0	0	0	(5,191,830)	0	(5,191,830)	
Total Amounts Held For Others	(7,355,225)	0	0	0	(190,322)	(7,545,547)	0	(7,545,547)	
Less: Subsequent OHCS Cash Needs									
Principal Due - Maturities & Calls - 7/1/2016 & 7/7/2016	0	0	(7,110,000)	(42,650,000)	(2,110,000)	(51,870,000)	0	(51,870,000)	
Accrued Interest Payable - 7/1/2016 & 7/7/2016	0	0	(2,232,079)	(6,545,207)	(2,606,453)	(11,383,739)	0	(11,383,739)	
Swap Payments - 7/1/2016	0	0	0	(2,743,784)	(222,078)	(2,965,862)	0	(2,965,862)	
Principal Due - Maturities & Calls - 8/1/2016 & 8/31/2016	0	0	0	0	0	0	(2,540,000)	(2,540,000)	
Accrued Interest Payable - 8/1/2016 & 8/31/2016	0	0	0	0	0	0	(1,276,894)	(1,276,894)	
Accounts & Other Payables	(260,941)	0	(44,628)	(291,000)	(1,140)	(597,709)	(28,975)	(626,684)	
Deferred LIHTC and Conduit Bond Fees	(1,250,741)	0	0	0	0	(1,250,741)	0	(1,250,741)	
Total Subsequent OHCS Cash Needs	(1,511,682)	0	(9,386,707)	(52,229,991)	(4,939,671)	(68,068,051)	(3,845,869)	(71,913,920)	
Less: Acquisition Funds (from Bond Proceeds)									
Acquisition Funds to be Loaned or Redeemed	0	0	0	(106,582,158)	0	(106,582,158)	0	(106,582,158)	
Total Acquisition Funds	0	0	0	(106,582,158)	0	(106,582,158)	0	(106,582,158)	
Less: Revenue Account Funds (from Bond Proceeds)									
Prepayments Held to Required Bond Redemptions	0	0	(3,464,762)	(15,639,383)	0	(19,104,145)	0	(19,104,145)	
Prepayments Held for Required Recycling	0	0	0	(26,955,165)	0	(26,955,165)	0	(26,955,165)	
Total Revenue Accounts Fund to Redeemed or Recycled	0	0	(3,464,762)	(42,594,548)	0	(46,059,310)	0	(46,059,310)	
Less: Indenture Reserves (from Bond Proceeds)									
Debt Reserve	0	0	(3,425,265)	(18,829,062)	(6,508,495)	(28,762,822)	(5,657,786)	(34,420,608)	
Total Reserves Funded from Bond Proceeds	0	0	(3,425,265)	(18,829,062)	(6,508,495)	(28,762,822)	(5,657,786)	(34,420,608)	
Less: Indenture Reserves (not from Bond Proceeds)									
General Reserve	0	0	(561,144)	0	0	(561,144)	0	(561,144)	
Insurance Reserve	0	0	0	(9,833,743)	0	(9,833,743)	0	(9,833,743)	
Mortgage Insurance Pool Reserve	0	0	0	(2,153,680)	0	(2,153,680)	0	(2,153,680)	
Total Indenture Reserves (not from Bond Proceeds)	0	0	(561,144)	(11,987,423)	0	(12,548,567)	0	(12,548,567)	
Less: Other Indenture Restrictions									
Dedicated Fund/Indenture	0	0	(3,124,026) (1)	0	0	(3,124,027)	(18,731,340) (2)	(21,855,369)	
Asset-to-Liability Test	0	0	0	(13,175,300) (3)	0	(13,175,303)	0	(13,175,303)	
Combined Program Account (3)	0	(18,673,546) (4)	0	0	0	(18,673,550)	0	(18,673,550)	
Total Other Restrictions	0	(18,673,546)	(3,124,026)	(13,175,300)	0	(34,972,880)	(18,731,340)	(53,704,222)	
Total Cash & Investments - Unrestricted	1,753,427	0	0	18,006,100	15,287,780	35,047,299	0	35,047,298	

(1) Housing Revenue Bonds were issued pursuant to the New Issue Bond Program ("NIBP") Agreement between OHCS and U.S. Treasury. In accordance with this Agreement, all distributions from this indenture require approval to the U.S. Treasury. Since its inception in December 2009, no distributions have been taken this indenture and current cash flows do not currently anticipate any future distributions occurring from this indenture.

(2) In accordance with Article XI-(2) of the Oregon Constitution, the funds within the Elderly & Disabled Housing Indenture are restricted for the purposes of elderly and disabled housing program. Section 5.4 (h) of the Indenture only allows "free and clear" distributions when amounts on deposit under the Indenture are sufficient to pay all outstanding bonds. Current cash flow analyses assume annual distributions for program purposes of \$1,500,000.

(3) Section 408 (ii) of the Mortgage Revenue Bond Indenture allows "free and clear" distributions from the Indenture only when cash flow analyses indicate that assets are 102% or more of liabilities. Distributions from this Indenture may only be used for Single-Family program expenses as prescribed in Section 408 (i) until 102% is achieved and maintained. Current cash flow analyses assume annual distributions for Single-Family of \$4,300,000. The restricted amount above reflects the 2% of assets in excess of liabilities required before "free and clear" distributions can be taken from the MRB indenture as of 6/30/2016.

(4) Section 3.2 of the Combined Program Account Indenture restricts the use of funds under the Indenture to 1) payment of debt service in certain bond programs (currently and 3) payment of program expenses under the Act (ORS 456.515 to 456.725). The pledge and continued growth of the Combined Program Account to the MRB Indenture is an integral factor in maintaining the current bond rating. The Combined Program Account is also a key factor in allowing the Department to maintain its "A2 (stable)" Department rating from Moody's.

OTHER FUNDS ENDING
BALANCES

OTHER FUNDS ENDING BALANCES: HOMELESS SERVICES PROGRAMS

- Limited
- Grant Funds

Treasury Fund Number	Treasury Fund Name	Statutory Reference	2015-17 Ending Balance Revised	2017-19 Ending Balance Revised
00615	EMERGENCY HOUSING ASSISTANCE ACCOUNT	ORS 458.620	\$1,070,369	\$794,228
01288	HOUSING PLUS 2008B - SUPPORTIVE SERVICES	ORS 456.576	\$447,288	\$0
01546	WILDFIRE DAMAGE HOUSING RELIEF ACCOUNT	ORS 458.620	\$50,529	\$0

OTHER FUNDS ENDING BALANCES: ENERGY SERVICES PROGRAMS

- Limited
- Grant Funds

Treasury Fund Number	Treasury Fund Name	Statutory Reference	2015-17 Ending Balance Revised	2017-19 Ending Balance Revised
00897	LOW-INCOME ELECRCIC BILL PYMT ASSISTANCE	ORS 456.587	\$6,517,427	\$2,097,346
00898	SB1149 ELECTRICITY PUBLIC PURPOSE CHARGE (ECHO program)	ORS 456.587	\$8,120,580	\$6,070,325
00898	SB1149 ELECTRICITY PUBLIC PURPOSE CHARGE (Multifamily Low Income Weatherization program)	ORS 456.587	\$9,603,263	\$5,747,656

OTHER FUNDS ENDING BALANCES: MULTIFAMILY RENTAL HOUSING

- Limited
- Grant Funds

Treasury Fund Number	Treasury Fund Name	Statutory Reference	2015-17 Ending Balance Revised	2017-19 Ending Balance Revised
00550	MOBILE HOME PARKS ACCOUNT (OMBUDSMAN)	ORS 446.525	\$1,294,743	\$1,400,902
00616	HOUSING DEVELOPMENT AND GUARANTEE ACCOUNT	ORS 458.620	\$1,983,932	\$1,447,237
00898	SB1149 ELECTRICITY PUBLIC PURPOSE CHARGE (Multifamily housing development)	ORS 456.587	\$10,889,215	\$8,167,011
00936	COMMUNITY DEVELOPMENT INCENTIVE PROJECT	ORS 458.720	\$1,264,473	\$0

OTHER FUNDS ENDING BALANCES: MULTIFAMILY RENTAL HOUSING

- Limited
- Grant Funds

Treasury Fund Number	Treasury Fund Name	Statutory Reference	2015-17 Ending Balance Revised	2017-19 Ending Balance Revised
01305	LRB 2009 A: HOUSING PLUS UNITS	ORS 456.576	\$278,934	\$0
01343	GENERAL HOUSING ACCOUNT	ORS 456.576	\$12,780,384	\$7,646,994
TBD	2015-17 Lottery bonds for Mental Health Housing	ORS 456.576	\$19,000,000	\$4,000,000
TBD	2015-17 Lottery bonds for Housing Preservation	ORS 456.576	\$6,090,585	\$689,159

OTHER FUNDS ENDING BALANCES: SINGLE FAMILY PROGRAMS

- Limited
- Grant Funds

Treasury Fund Number	Treasury Fund Name	Statutory Reference	2015-17 Ending Balance Revised	2017-19 Ending Balance Revised
00695	HOME OWNERSHIP ASSISTANCE ACCOUNT	ORS 458.620	\$3,429,320	\$1,352,342

OTHER FUNDS ENDING BALANCES: CENTRAL SERVICES

- Limited
- Operating Funds

Treasury Fund Number	Treasury Fund Name	Statutory Reference	2015-17 Ending Balance Revised	2017-19 Ending Balance Revised
00401	OTHER FUNDS - HOUSING PROGRAMS (Operating Account)	ORS 456.576	\$2,200,000	\$2,200,000

OTHER FUNDS ENDING BALANCES: BOND RELATED ACTIVITIES

- Limited
- Operating Funds

Treasury Fund Number	Treasury Fund Name	Statutory reference	2013-15 Ending Balance Revised	2015-17 Ending Balance Revised
00431	HOUSING FINANCE ACCOUNT	ORS 456.720	\$600,000	\$600,000
00477	ELDERLY and DISABLED OPERATING FUND	Article XI-1, ORS 456.535, BOND INDENTURE	\$400,000	\$400,000

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**COMMUNICATION WITH THOSE CHARGED WITH GOVERNANCE
For the Oregon Housing and Community Services Enterprise Funds
and Selected Statewide Audit Accounts**

To the Oregon Housing Stability Council and the Management of Oregon Housing and Community Services:

We have audited the financial statements of the Elderly and Disabled Housing Fund and the Housing Finance Fund, enterprise funds of the State of Oregon, Housing and Community Services Department ("department"), as of and for the year ended June 30, 2016, and have issued our report thereon dated November 10, 2016. We have also audited the rental assistance expenditures account in the rental assistance fund (GAAP fund 1112) as part of the Statewide Audit of the State of Oregon's Comprehensive Annual Financial Report. Professional standards require that we provide you with the following information related to our audit.

**Our Responsibility under Auditing Standards
Generally Accepted in the United States of America**

Our responsibility, as described by professional standards, is to form and express an opinion about whether the financial statements prepared by management are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States. Our audit of the financial statements does not relieve you or management of your responsibilities.

Our responsibility is to plan and perform the audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits in *Government Auditing Standards*, and to design the audit to obtain reasonable, rather than absolute, assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the department's internal control over financial reporting. Accordingly, we considered internal control solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are also responsible for communicating significant matters related to the audit that, in our professional judgment, are relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures for the purpose of identifying other matters to communicate to you.

Planned Scope and Timing of the Audits

We performed the audits according to the planned scope and timing previously communicated via our engagement letter and discussion with management during our audit.

Significant Findings or Issues

We did not identify any significant findings as a result of our audit.

Qualitative Aspects of Accounting Practices

Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the department are described in Note 1 to the financial statements. No new accounting policies were adopted and there were no changes in the application of existing policies during the fiscal year. We noted no transactions entered into by the department during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements/records in a different period than when the transaction occurred.

Financial Statement Disclosures

The disclosures in the financial statements, and the disclosures prepared by management and provided to SARS for inclusion in the State of Oregon CAFR, are consistent, clear and understandable.

Significant Difficulties Encountered During the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all factual, projected, and judgmental misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. We did not identify any misstatements during our audit.

Disagreements with Management

For purposes of this letter, professional standards define a disagreement with management as a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Other Findings or Issues

No other findings or issues came to our attention that are significant and relevant to those charged with governance regarding their responsibility to oversee the financial reporting process.

Management Representations

We have requested and received certain written representations from management that are included in the management representation letter dated November 10, 2016.

Management Consultation with Other Independent Auditors

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. To our knowledge, there were no such consultations with other accountants.

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This communication is intended solely for the information and use of the Oregon Housing Stability Council and management of the department and is not intended to be and should not be used by anyone other than these specified parties.

Office of the Secretary of State, Audits Division

STATE OF OREGON
November 21, 2016

Secretary of State Audit Report

Jeanne P. Atkins, Secretary of State

Mary Wenger, Interim Director, Audits Division



Oregon Housing and Community Services: Critical Improvements Needed to Help Ensure Preservation of Affordable Housing for Low-Income Oregonians

Executive Summary

Oregon is in a housing crisis—housing costs are high, vacancy rates are low, and low-income Oregonians struggle to find affordable housing. Oregon Housing and Community Services (OHCS) is charged with being the state’s leader in housing, but challenges are hindering its progress in helping to address the affordable housing crisis.

We found OHCS should improve its affordable housing preservation efforts, strategic planning, and data management. In addition, OHCS should address organizational challenges, which include poor communication, inconsistent staffing levels, and inadequate policies and procedures. By improving in these areas, OHCS will be better able to help ensure affordable housing for low-income Oregonians.

Affordable housing is essential to meet Oregon’s low-income housing needs



Increasing costs, combined with relatively stagnant incomes since the 2008 recession, have resulted in housing costs taking a bigger chunk of Oregonians’ paychecks.

Because the housing market generally does not produce new housing affordable to households making less than 60% of median income, federal, state and local governments work with nonprofit organizations and for-profit developers to create affordable housing for this segment of the population.

Housing subsidies that keep rents affordable for low-income Oregonians are important. A substantial amount of affordable housing could be lost in the next 20 years by way of expiring federal rent subsidies, use restrictions, maturing mortgages and/or deterioration.

Loss of affordable housing damages progress on meeting overall housing needs for the state. The loss of even a single rental unit could mean one more Oregon family may not be able to find a home.

Agency efforts to preserve affordable housing fall short



Affordable rental housing created with government subsidies is the main focus of our report. We found the agency could improve its housing planning and preservation of this existing low-income affordable housing.

Since 1991, OHCS has been required to complete an annual comprehensive plan for the state, detailing the housing needs of Oregonians. Thus far, statewide housing planning has come up short. Agency leadership is working to build on existing needs assessments and planning to create a comprehensive plan for the state. A major hurdle to achieving this goal is the lack of an accurate and reliable inventory of affordable housing, another task the agency is currently working to complete.

Preserving federal rent subsidies is critical to helping preserve low-income affordable housing. It cannot be achieved without a variety of public and private partners working together collaboratively. Poor external communication aggravated strained relationships with housing developers and partners in the housing community. Although improved, OHCS could do more to strengthen relationships with partners.

OHCS could also work with funders in the state to better align funding cycles and application processes so preservation projects go more smoothly. Many housing developers rely on OHCS funding each year to build or preserve affordable housing, making OHCS a key partner. For developers investing millions of dollars and several years into projects, predictability and transparency are important. Clear funding priorities will help developers understand and plan for the affordable housing that OHCS is targeting.

Oregon also falls behind other states in providing funding developers need to make projects viable. Increased gap funding could expand the use of a tax credit program OHCS administers, resulting in preserving more low-income affordable housing.

Strategic planning is not sufficient

The Oregon Legislature tasked OHCS with leading the state in housing policy and serving as the central source of affordable housing data, training and technical information. We found that OHCS is not achieving these expectations.

The agency needs to improve its strategic planning to better provide for affordable housing in the state. Without adequate strategic planning, OHCS' vision for the future and priorities are unclear, potentially resulting in the loss of affordable housing. Improved planning, including setting measurable goals, will help OHCS identify priorities, recognize success, detect problems and respond with corrective action.

Better data management needed for informed decision-making

The lack of complete and accurate data on the multifamily affordable housing portfolio kept us from completing planned work related to affordable housing. This included evaluating the effects of OHCS policies as well as overall trends of properties in need of preservation.

The agency could do much better at using data to inform decision-making. Due to inadequate resources dedicated to data systems and data management over a number of years, the systems are outdated, not integrated, and require workarounds. OHCS could benefit from an integrated data system that tracks projects from beginning to end. This would eliminate the workarounds that contribute to errors, incomplete data, and other problems we identified.

OHCS could also improve its collection and use of financial data from its affordable housing projects in order to help identify best practices. Such a system was in place, but was discontinued by agency leadership in 2012 and to date, has not been replaced.

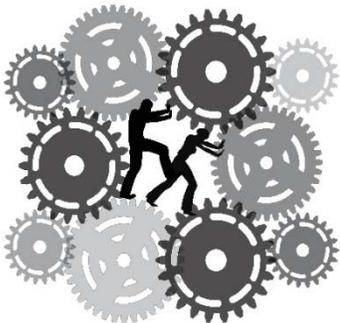
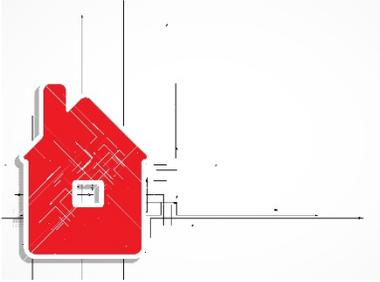
Organizational challenges impede agency from addressing affordable housing

We identified organizational issues affecting all sections of the agency that impede OHCS efforts to adequately address affordable housing, including preserving low-income affordable housing. These challenges include poor communication, inconsistent staffing levels, and inadequate policies and procedures.

We found significant issues with both OHCS' tone at the top and internal communication. Both are influenced by leadership's operating style and management philosophy, among other things. More importantly, both are critical to enabling the agency to be successful at managing its priorities. To gain a better understanding of the agency work environment, we conducted a survey of agency staff. Overall, survey results indicate that significant communication issues exist between agency leadership and staff.

OHCS has also experienced capacity issues, such as loss of institutional knowledge due to turnover and agency restructuring. At the same time, the workload in the agency's Multifamily Section has increased. The current workload and capacity leaves little time to analyze decision-making and data to improve administrative systems and bolster better policy. Having a better understanding of workflow and resources will help identify capacity for additional work and target areas in need of additional staff or resources.

In addition, we found that some agency policies and procedures were absent, outdated, or weak. For example, OHCS does not have standardized or written contracting and procurement policies, resulting in inconsistent practices.



Recommendations

To help ensure affordable housing for low-income Oregonians, we recommend OHCS management improve housing preservation efforts, strategic planning, and data management. We also recommend OHCS management address organizational challenges including organizational culture, communication with staff and stakeholders, workflow and capacity issues, and inadequate policies and procedures.

Our detailed recommendations for agency management are included on Page 31.

Agency Response

Oregon Housing and Community Services management generally agrees with the findings and recommendations in this report. The full agency response can be found at the end of the report.

Background

Housing costs are rising



Oregon is in a housing crisis. Housing costs are high, vacancy rates are low, and low-income Oregonians struggle to find rental units they can afford.

From July 2015 to July 2016, home values in the state rose 12.5% while rental housing is currently increasing nearly 7% a month.

Increasing costs, combined with relatively stagnant incomes since the 2008 recession, result in housing costs taking a bigger chunk of Oregonians' paychecks. According to Oregon Housing and Community Services (OHCS) 77% of Oregonians making \$25,000 or less are "rent-burdened," which means they spend 30% or more of their income for housing.

Overall, Oregon's vacancy rates are currently much lower than the 5% vacancy that is typically expected in a balanced market. Low vacancy rates limit housing availability and drive up prices. For example, rates in Deschutes, Crook, and Jefferson counties are as low as .5% and are only slightly better in Jackson County at 1.4%. In the Portland Metro area, vacancy rates of late have increased to around 6%—though rates by neighborhood vary.

Generally, the housing market does not produce new housing affordable to households making less than 60% of median income—about \$40,000 for a family of three or \$30,000 for a single person household. As a result, federal, state and local governments work with nonprofit organizations and for-profit developers to create affordable housing for this segment of the population. This housing is comprised of rental units created with government subsidies.

In 2015, Oregon ranked:

- 1st for unsheltered families with children
 - 1st in the rise of chronic homelessness
 - 2nd highest in unsheltered homeless—meaning people are living on the streets, in cars, or other places not meant for human habitation
 - 3rd in the rise of overall homelessness
 - Portland Metro ranked 8th in chronically homeless compared to other metro areas
-

Homelessness, poverty and housing are linked

Those experiencing poverty are frequently unable to pay for housing and other necessities like food, childcare, health care, or education. They must make difficult choices when limited resources cover only some of these necessities.

A growing shortage of affordable rental housing has been attributed to the rise in homelessness. Oregon is doing poorly on key indicators of homelessness, ranking high when compared to other states and national averages.

Oregon's non-metro areas had the third largest number of homeless Oregonians when compared with similar regions. In some rural areas, housing is simply not available. Community Action Agencies (CAAs), which address housing stabilization issues, are struggling to find housing for their clients. One rural CAA director said her agency had over 50 families unable to find housing.

Preserving affordable rental housing is important

Affordable rental housing in Oregon is subsidized by federal and state programs. A substantial amount of this housing could be lost in the next 20 years by way of expiring federal rent subsidies, use restrictions, maturing mortgages and/or deterioration. Preserving affordable housing means ensuring rents stay affordable for low-income earners so they can stay in their homes. Properties can be preserved when they are refinanced to extend affordability or when federal rent subsidies are renewed. At the same time, they are typically rehabilitated.

Existing affordable housing represents a substantial public investment. Preserving the federal rent subsidies that keep rents affordable for low-income Oregonians is important, as there are no new subsidies of this kind. If the assistance is not renewed for a given property, it may revert to market rents, which current low-income tenants may not be able to afford.

Federal funding for housing is a web of programs that includes subsidies from the U.S. Department of Housing and Urban Development (HUD), the U.S. Department of Agriculture Rural Development (RD), and the Internal Revenue Service (IRS). Subsidies like loans, mortgage insurance, and rental assistance encouraged private housing developers to create affordable housing beginning in the 1950s. Most HUD and RD housing was developed in the late 1960s through the mid-1980s. Currently, the main federal support for affordable housing is the Low Income Housing Tax Credit program, created in 1986 by the IRS.

Loss of affordable housing undermines progress on meeting overall housing need for the state. The loss of even a single unit of housing could mean one more Oregon family cannot find a home.

HUD properties at risk of loss and deterioration

The federal government first created national housing programs in the 1930s. In the late 1950s and into the 1960s, HUD and its predecessor created housing programs that subsidized privately owned properties through mortgage insurance and low-interest rate loans. In exchange, property owners offered lower rents. HUD also created the first rental assistance program in 1974, known as project-based Section 8, which pays owners the difference between what tenants pay (30% of their income) and fair market rent. Although the program officially terminated in 1983, legislation has continued these subsidies in existing projects. Nearly half of those receiving project-based Section 8 in Oregon are seniors or people with disabilities, and 73% are considered extremely low-income, with the average household income in 2015 at \$11,500.

According to HUD data, there are 325 HUD properties in Oregon. Of these, 121 properties (4,000 rental units) have Section 8 rental assistance expiring between 2016 and 2024. Owners may renew the subsidies through contracts lasting 1, 5, or 20 years. Many Oregon owners have

Depending on the program, property owners are required to maintain property affordability for 15-60 years.

renewed for just 1 or 5 years. This keeps their options open should they decide to rent at market rates, sell the property, or recapitalize the project to extend contracts for a longer period.

Determining the number of HUD properties at risk for conversion to the private market is challenging given available data, as each property would need to be examined individually to determine its risk factors. Though not at risk of losing subsidies, there are an additional 72 HUD administered properties with 2,204 rental units, at risk of deterioration due to age and inability to take on debt to recapitalize and renovate.

USDA Rural Development portfolio is aging

Rural Development (RD) started its rural rental housing loan program in 1963. Close to a decade later, RD changed program rules to spur private sector participation, in addition to nonprofit property owners. Following this expansion, RD programs grew rapidly.

According to the Oregon RD office, there are 190 RD projects in Oregon, which includes 202 properties and over 6,000 rental units. These properties are aging, as many were built in the 1970s and 1980s. RD properties house some of Oregon's most vulnerable. Sixty-one percent of RD renters are seniors and people with disabilities.

Historically, there have been challenges with accurate and reliable RD data. This led to a Government Accountability Office audit to determine the number of maturing RD mortgages in the next 10 years and the properties at risk of losing affordability. In September 2016, the USDA released new data showing 18 RD properties (232 rental units) in Oregon with expiring mortgages between 2016 and 2027. There are also 74 properties (1,226 units with rental assistance) eligible to pre-pay their mortgages. When RD mortgages are pre-paid, the units lose federal rent subsidies and affordability.

Unknown number of Oregon LIHTC properties in need of preservation

The Low Income Housing Tax Credit (LIHTC) program is the primary program developers use to fund preservation and rehabilitation projects of HUD and RD properties. This program is also used to finance new construction of affordable housing. It incentivizes housing developers to create rental units affordable to those earning 60% or less of the Area Median Income. From its inception through 2014, the program created or preserved nearly 3 million multifamily rental units. In Oregon, 38,783 rental units were created or preserved in the same period.

There are two different types of tax credits—9% and 4%. Both are used for preserving and rehabilitating affordable housing and to finance new construction of affordable housing. OHCS awards the 9% tax credit to housing developers each year through a competitive process, called the Notice of Funding Availability (NOFA). The 4% tax credits are allocated through a noncompetitive process and half the project must be funded with tax-exempt private activity bonds. In Oregon, projects funded with the 9%

When mortgages mature, or expire, subsidies are lost and owners are no longer required to keep them affordable.

tax credit must remain affordable for 60 years and projects funded with the 4% must generally remain affordable for 30 years. Another difference is that projects awarded the 9% tax credit produce more funding than projects awarded the 4% tax credit. Funding for projects beyond the tax credits comes from developer investment and gap financing such as loans or grants.

LIHTC properties are also at risk. When affordability periods end, property owners can keep properties affordable without new subsidies, apply for new tax credits, or opt out of the LIHTC program and convert to market-rate housing. LIHTC properties can also be at risk of deterioration when rents are not sufficient to maintain properties. Properties may need significant repairs or modernization beyond the financial capability of the owners, such as replacing building siding or rehabbing kitchens. Without rehabilitation, some Oregonians may be at risk of living in sub-standard housing.

Although OHCS maintains a listing of LIHTC properties in Oregon, we were not able to verify its accuracy due to problems with the Housing Finance Division's data systems. Also, while the agency inspects LIHTC properties annually to determine their performance, including physical condition, a database that records properties at risk of deterioration was still being developed during our audit.

Oregon Housing and Community Services created to be the state leader on housing



OHCS was created in 1971 to set overall housing policy and to serve as a central source of training, housing and technical information. Some of its original duties included administering interest free loans to nonprofit housing sponsors, coordinating federal housing programs, developing policies to increase low-income housing, and advising state and local governments about actions affecting the cost or supply of housing.

The Oregon Housing Council, also established in 1971, advises and oversees OHCS. The Council also develops program guidelines, provides policy direction and budgetary oversight, and approves financial transactions such as loans, grants, and tax credits. In 2016, HB2442 transitioned the Council from an advisory board to a policy-setting board, now referred to as the Housing Stability Council. In the same legislation, other OHCS advisory boards were disbanded with the Council absorbing their responsibilities.

The Community Action Partnership of Oregon (CAPO), comprised of directors of Community Action Agencies, provides advice and recommendations regarding administration and funding of antipoverty programs.

OHCS mission: *We provide stable and affordable housing and engage leaders to develop integrated statewide policy that addresses poverty and provides opportunity for Oregonians.*

OHCS vision: *All Oregonians have the opportunity to pursue prosperity and live free from poverty.*

Financing housing and providing stability to vulnerable populations

OHCS is divided into two major divisions—Housing Finance and Housing Stabilization. Housing Finance, which has about \$12 million in operating costs and \$349 million in program payments in the 2015-17 biennium, administers programs related to:

- debt management;
- multifamily programs and lending including the LIHTC program;
- homeownership programs and single family lending;
- asset management and compliance, including monitoring properties the agency has funded; and
- the Oregon Homeownership Stabilization Initiative, which implements foreclosure prevention programs.

The Multifamily Section, located within the Housing Finance Division, administers the department's low-interest loan programs, grants, and tax credit programs for the purpose of developing or preserving affordable multifamily rental projects.

The Housing Stabilization Division administers programs that aim to prevent and end homelessness, and provide energy and weatherization services. These programs are primarily delivered through grants and contracts with community partners. Staff in this division also oversee the HUD project based Section 8 contract administration for the state. The division has about \$6 million in biennial operating costs and \$283 million in program payments.

Expanding responsibilities and shrinking resources

In the years following OHCS' creation, programs were added and expanded, growing its responsibilities. In 1987, OHCS became Oregon's independent housing finance agency administering the LIHTC program.

In 1991, the agency merged with the Community Services Division, doubling in size and broadening its mission by adding homelessness and food assistance programs. More state and federal programs were added through the 1990s, including the Housing Development Guarantee Grant Program, Emergency Housing Assistance to homeless persons, and the Oregon Rural Rehabilitation Program for farmworker housing. In addition, OHCS oversees the Oregon Volunteers program, which administers Court Appointed Special Advocates for children.

By 2001, OHCS administered 37 programs. The agency continued to pursue and received funding for new programs, and was assigned additional programs by the Legislature. By the 2009-11 biennium, the agency was responsible for administering approximately 50 programs.

In 2013, our audit of OHCS recommended the agency evaluate the benefits and costs of reducing duplication, overlap and fragmentation among its

programs. In 2016, the Legislature moved food assistance programs to other agencies, leaving OHCS still operating 49 other programs.

Most of the agency's programs are funded with federal and other funds. State general funds account for only about 1% of the agency's budget.

In the past, OHCS used distributions of revenues from Multifamily and Single family housing bond-financed loan programs to subsidize administrative costs of other programs, such as food and rent assistance. In the 2011-13 biennium, these distributions subsidized more than 25% of the other programs' administrative costs. This included 100% of administrative costs for the Low Income Rental Housing Assistance program and over 90% of these costs for the Vertical Housing Program. Administering these other programs became fiscally unsustainable for the agency, as available revenues significantly decreased due to economic factors. In 2016, the agency made progress identifying and aligning funding sources as part of an effort to become more fiscally sustainable.

For years, the Oregon Volunteers program had been subsidized with other agency funds. For the first time since acquiring the program, OHCS obtained general funds for Oregon Volunteers' administrative expenses in the 2015-2017 biennium.

OHCS experienced a significant amount of organizational change

2011

- October | *New Director*
- November | *Portland Office Closes*

2012

- January | *1st Restructuring*
- April | *New Executive Team*

2013

- February | *Transition Planning Begins*

2014

- February | *Transition Plan to Legislature*
- March | *Strategic Planning Begins*
- July | *2nd Restructuring*
- September | *Strategic Operations Plan*
- November | *3rd Restructuring*

2016

- January | *HB2442, strengthening Housing Stability Council*
- May | *Director Resigned*
- November | *New Director*

Over the last five years, OHCS has experienced significant change, impacting workload and contributing to low staff morale.

Many changes began as efforts to bring the agency's expenses in line with revenue. In October 2011, a new director was appointed to address these financial challenges and determine if the agency should be dismantled. The director removed 12 positions in 2011, eliminating their duties or shifting them to other staff. Half of these positions were management positions. Other positions such as the internal auditor, were left unfilled. In January 2012, the director restructured the department, dividing the agency into three divisions: policy, business operations, and program delivery. By April, an entirely new executive team was in place. In late 2013, the director recommended the agency remain intact.

However, uncertainty about the agency's future continued. The agency's funding for the second year of the 2013-2015 biennium was withheld by the Legislature, pending a report by the director on sustainable program delivery. As part of this task, management developed a transition plan to move the agency toward improved service delivery, effectiveness, and fiscal sustainability, which they presented to the Legislature in 2014. Following this, the Legislature approved the second year's funding.

Shortly afterward, executive management began strategic planning. In July of that year, management presented a newly created mission and vision for

the agency. That same month, the director restructured divisions within the agency again.

In November 2014, the director restructured the agency for the third time into its current structure. As noted above, legislation passed in January 2016 changed the role of the Housing Stability Council from an advisory board to a governing and policy-setting board. During the course of our audit, the agency's director resigned and an interim director was appointed. A new director began November 1, 2016, shortly before the release of this audit.

Audit Results

Agency efforts to preserve affordable housing fall short



OHCS could do more to preserve affordable housing for low-income Oregonians. To effectively address preservation and affordable housing needs in the state, the agency should improve its housing planning and relationships with housing partners.

OHCS management has not completed a housing plan that details the state's housing supply, needs, and resources—all essential for effective affordable housing leadership. To successfully plan, the agency should have a complete inventory of affordable housing along with an updated assessment of housing needs in the state.

Relationships with partners are also essential to preserving affordable housing, and OHCS could do more to strengthen relationships and communication with its partners. In addition, OHCS could work with other funders in the state to better align funding cycles and application processes so that preservation projects go more smoothly. Clear funding priorities will help developers better understand, and plan for, the affordable housing OHCS is targeting. Expanding the use of federal and state tax credit programs will also help preservation efforts.

Comprehensive statewide housing plan is incomplete

Since 1991, state statute has required OHCS to prepare a comprehensive state plan for housing. The statute clearly states the state housing plan should include an inventory of affordable housing, and information on market and inventory conditions, population trends, household composition and housing conditions. In addition, the plan is to include an accurate picture of the affordable housing in the state, or at a minimum, OHCS' own inventory. The plan should also include a needs assessment that summarizes data on the housing needs of homeless and income-eligible families.

OHCS leadership explained that their Consolidated Plan is the agency's effort to fulfill the statute. However, because the plan is written specifically to show how OHCS uses HUD administered dollars, it does not represent a complete view of the state's housing needs and resources. Though the Consolidated Plan has fulfilled all the HUD requirements, it falls short of a comprehensive state plan as described in statute.

The Consolidated Plan lacks clear implementation strategies to achieve goals. For example, preservation is identified as a high priority, but the plan lacks a roadmap of how to get there. It also does not specify the number, type and location of rental units the agency intends to preserve. Without

clearly defined goals and information, it is difficult to measure how well OHCS is doing at preserving affordable housing in the state.

Other housing information in the Consolidated Plan is incomplete. Its statewide data does not account for significant differences in housing issues between regions, counties, cities or municipalities. It lacks a review of all financial resources, as required by statute. Financial resources reviewed in the plan are limited to four HUD administered programs and several OHCS programs. In addition, local and private funding sources are not reviewed.

Though the agency does not have a comprehensive state plan, management reports staff are building on the Consolidated Plan to create one.

Oregon does not have a complete statewide housing inventory

A single reliable source of data for properties is an essential management tool for any housing finance agency. This is important information for the comprehensive statewide plan. A complete inventory allows a state to identify its housing and preservation challenges and prioritize where action is needed, both at the property level—to determine properties that need to be contacted and offered incentives to remain affordable—and at the community level—to identify neighborhoods to target for preservation of affordable rental housing. For example, officials in Florida use state and federal data to create a comprehensive database of affordable housing to aid planning efforts.

A complete inventory should include basic characteristics of the subsidized housing portfolio including:

- property name and address;
- housing type or target population, such as income-level;
- total number of rental units and number of affordable units;
- years affordability restrictions begin and expire;
- funding sources; and
- physical condition of the property.

Although OHCS does maintain an affordable housing inventory, they are working to make it more complete. The most recent affordable housing inventory was used in 2016 to score applicants on the 9% LIHTC application. In addition to being incomplete, the inventory had multiple errors. For example, we learned the data was not vetted with partners to ensure accuracy before it was published. One housing provider told us the inventory showed a property for their organization that did not exist.

Although Preserve Oregon, a nonprofit program, maintains the most comprehensive inventory database of affordable housing in the state, staff who maintain the database stated they cannot guarantee its accuracy because it is based on publically available data, including OHCS data. The database also does not offer the property-level data OHCS needs to inform their planning efforts.

Components of a Comprehensive Housing Needs Assessment

- Demographic data
 - Economic trends
 - Housing inventory
 - Housing need by region and population
 - Policies and incentives
 - Community services
 - Input of stakeholders
 - Recommendations on how to achieve housing goals
-

Housing needs assessment could be improved

A thorough assessment of housing needs is an important element of any comprehensive state housing plan. A needs assessment is a systematic process for determining and addressing gaps between current conditions and desired conditions.

While the current OHCS Consolidated Plan contains a section on housing needs in the state, it does not include an analysis of the current housing supply, an essential element.

The current needs assessment would also benefit from updated and improved demographic data. OHCS management told us the assessment lacked statewide data and included outdated data. The information in the assessment for 2016-2020 is based, in large part, on HUD data from 2007-2011. Community needs surveys and assessments from various counties are used, but may not be thorough or current in all areas of the state. For example, we heard from some housing development leaders that communities lack capacity and resources to put together updated needs assessments. In addition, the OHCS current needs assessment relies heavily on estimates of poverty and housing cost burden, but lacks actual numbers of Oregon families or individuals in need of housing, type of housing they need, and in which areas of the state.

In our interviews with other state housing finance agencies, we found examples of needs assessments that better inform statewide housing plans and help decision makers direct funding to the most critical areas. Delaware's 2014 Needs Assessment revealed two categories of housing needs: elderly low-income and coastal market-rate housing for retirees. The assessment also showed an aging housing inventory at risk of becoming unaffordable. As a result, the state continued to make preservation a high priority.

A more thorough understanding of low-income housing needs in the state would help OHCS better target resources to meet regional needs, and those of special populations, such as elderly Oregonians or veterans.

Stronger partnerships beneficial to preservation efforts

Preserving federal housing subsidies cannot be achieved without a variety of public and private partners working together collaboratively. Stronger relationships with consistent communication would help the agency better understand preservation needs across the state and plan accordingly. Although OHCS has had successful partnerships in preservation initiatives, there is room for the agency to strengthen its relationship and communication with its partners.

In 2007, OHCS, the Portland Housing Bureau, and other partners began working on strategies to preserve properties. A nonprofit organization, Network for Oregon Affordable Housing, administered the effort called Preserve Oregon. It included a new fund to support purchases of properties

at-risk of losing their affordability. OHCS contributed an initial \$1 million but has not contributed since.



Exterior of Bronaugh Apartments, a property rehabilitated and its subsidies preserved as part of the 11x13 campaign.

In 2008, the Portland Housing Bureau began an initiative, called the 11x13 Preservation Campaign, to preserve 11 privately owned buildings at risk of losing HUD rental subsidies by 2013. Because of their desirable location, many of the properties were at risk of being converted to market-rate condominiums, which would have displaced hundreds of very low-income residents, many of whom were elderly or disabled. For its part, OHCS provided valuable funding through the LIHTC program, Housing Preservation Fund, and Multifamily Weatherization program. When it was completed, the Portland Housing Bureau and partners were able to preserve 700 rental units in 11 buildings for another 60 years of affordability, allowing residents to stay in their homes.

Outside of these larger initiatives, OHCS has struggled to maintain working relationships with partners. USDA's Rural Development (RD) is a key partner in preservation efforts, but we found communication and collaboration between RD and OHCS to be minimal and, at times, strained. In 2012, OHCS included a signed agreement with RD in the LIHTC Qualified Allocation Plan. The agreement established the conditions for cooperation, information exchange, and program support. However, the formal agreement appeared to end within a year and does not appear in subsequent LIHTC documents. With the lapse of the agreement, communication between the agencies became infrequent and coordination suffered.

Similarly, the OHCS-HUD relationship needs strengthening. HUD officials told us they had a positive working relationship with OHCS but they welcomed a closer working relationship with OHCS staff to share innovative ideas as well as some lessons learned.

When OHCS eliminated the five Regional Advisor positions, they were replaced with two housing integrators. However, their functions differ and there appears to be a lack of understanding with partners on where to go for capacity building and technical assistance, which agency leadership states could be a communication issue.

An example of successful collaboration comes from Georgia's Housing Finance Agency, which worked with funders and partners to develop a three-year program to help smaller, mostly rural communities create and launch a locally based plan to meet their housing and neighborhood revitalization needs. As part of this program, partners receive training and technical assistance.

Developers across Oregon told us they would like a closer, more positive working relationship with OHCS, but feel strained staff capacity and a history of mistrust prevents it.

OHCS acknowledges issues with external communication

Agency management acknowledges the need for transparent and consistent communication to build credibility with stakeholders. Effective external communication ensures important information comes in, while making sure relevant information flows out. Though improved, poor external communication has aggravated strained relationships with housing developers and partners in the housing community. OHCS administers a customer service survey to their partners on a semiannual basis, which for years has shown frustration with communication.

In both the 2016 OHCS customer service survey and in our conversations with partners, we found they truly desire collaboration and partnership with the agency, but do not feel they are getting it. One respondent said they felt like a problem to be dealt with, rather than a partner.

In addition, stakeholders reported not receiving timely information or responses to questions from staff; some said they simply never received answers. Respondents to the 2016 customer service survey also reported they did not feel the agency was transparent, a concern we heard during interviews.

Management's elimination of the five Regional Advisor positions in 2014 was a major setback to external communication. This change eliminated the primary mechanism for two-way communication between OHCS and partners and added to the workload of Multifamily and Asset Management and Compliance staff who became responsible for responding to housing developer and other stakeholder questions. Continued problems with communication can be seen in the results of a survey we conducted of OHCS staff in 2016. Just 52% of staff thought information and communication flowed well from partners to OHCS, and only 61% thought it flowed well from OHCS to partners.

Other states facilitate communication more effectively. In Minnesota, a Preservation Manager monitors and coordinates preservation efforts with stakeholders to help ensure long-term success of preservation efforts across the state.

Streamlining and coordinating processes could help preservation projects run smoothly

Intentional and consistent processes could also help with funding for preservation. When developers apply for funding, they often apply for local, state, and federal funding—each with a different application process and deadline. Disjointed timelines between funding streams can be a significant challenge for developers, especially those working on preservation projects. In early 2016, four RD-approved preservation projects were placed on hold because developers needed additional funds from the 9% LIHTC program before the projects could be completed. A significant delay in the release of the LIHTC funding resulted in developers having to reapply for their RD funding, which had expired due to the lengthy delay.

We found that a number of other states streamline and coordinate the application process. In Washington, local jurisdictions and the state housing finance agency created a joint system for applications and reporting. Montana created a uniform application as a one-stop shop for state housing loans, grants, and tax credits.

Frequent LIHTC policy shifts make it difficult for developers to plan

For developers investing millions of dollars and years into developing potential preservation projects, predictability and transparency are important, especially in the LIHTC program. Each year OHCS must make decisions on how to allocate tax credits, and in recent years, they have not always been consistent. Developers find the inconsistency frustrating and challenging to deal with, given the time and money necessary to make projects viable.

“It is hard to nail down [the agency’s] priorities. The only real way is to look at what they fund.”

-OHCS partner

In the absence of adequate housing planning, developers look to how OHCS spends their money to determine agency priorities and predict whether their proposed projects will receive funding.

The LIHTC program provides \$8.7 million to the state per year in federal tax credits and is one of the largest, most consistent funding sources at the agency’s disposal. OHCS determines how the credits are allocated, including how much is set aside for preservation projects. Each year, OHCS publishes its allocation criteria in one or more documents: the Qualified Allocation Plan (QAP), LIHTC Program Manual, and the Notice of Funding Availability (NOFA). Our review of 2012-2016 documents showed frequently changing criteria, priorities, and allocation scoring methods.

OHCS has inconsistently allocated the 9% LIHTC program funding to preservation projects, making it difficult for developers to plan their affordable housing projects. In 2010, OHCS set aside 50% of its federal tax credit allocation for preservation projects. In 2012, the preservation set-aside was reduced to 25% and in 2013, it was removed completely. In 2014, there was no mention of any preservation set-aside in its published allocation plan. However, in response to a letter from a stakeholder, OHCS clarified there was a 35% preservation set-aside and attached the response to the published plan. In 2016, the 35% set-aside was clearly stated in the published allocation plan.

Aware of developer’s concerns, OHCS tried to provide stability and predictability by keeping the 2015 published plan, manual and application the same as 2014. However, the stability did not last long. In response to stakeholder feedback, OHCS made significant changes to the 2016 allocation plan, which drives the scoring and allocation process. Developers told us this caused more confusion and frustration. To address stakeholder concerns regarding the 2016 plan, OHCS took additional time making revisions, resulting in an 18-month delay between LIHTC project awards. Because many developers rely on LIHTC funding for projects, this stalled many of the state’s affordable housing projects. Moving forward, the agency intends to provide consistency and predictability.

Housing finance agencies with more robust and comprehensive housing planning address preservation in a more stable way. Their plans lay out long-term strategies for preserving affordable housing in their states, clearly stating priorities on which to base changes. If changes are needed to allocation criteria, they can be based on the plans. Minnesota publishes their allocation plan one year in advance to allow enough time for developers to plan their projects. Utah eases developers into major changes by beginning conversations with developers two years in advance.

OHCS' attempts to address Oregon's unique geographic needs affect preservation efforts

Housing challenges vary throughout the state. For example, in Beaverton, there is little land available for development. In coastal areas such as Yachats, communities struggle to balance permanent housing with vacation rentals. In Island City, a small community near La Grande, demand for workforce and affordable housing is high. Low-income renters in Pendleton struggle to afford even affordable housing. Due to their housing crises, Portland and Bend declared housing state of emergencies in 2016.

In an attempt to use the 9% LIHTC program to address differing needs across Oregon, OHCS began dividing funding between five geographic regions in 2013: Central Oregon, Eastern Oregon, Metro Oregon, Southern Oregon, and the Valley/North Coast. The tax credit was meant to be equitably distributed across the state based on percentage of need. The results of the "need" formula showed that the Central and Eastern regions did not have enough "percentage of need" to allocate credits to fund a full project. To alleviate this, OHCS set a minimum credit amount for the Central and Eastern regions. This meant reallocating credits from other regions.

In a second attempt to more equitably address varying needs across the state, OHCS decided to align their geographic LIHTC distribution method with HUD's funding allocation strategy. In 2014 and continuing today, the state was divided into three geographical regions: Metro Oregon, Non-Metro HUD HOME participating jurisdictions, and the Balance of State.

Shifting to three geographic regions may have a disparate impact on RD preservation efforts. Developers of most RD projects in need of preservation are likely to apply for LIHTC funding and are likely to be in the Balance of State. Based on the latest 2016 LIHTC allocation method, the Balance of State region is allocated \$3.2 million of which \$1.1 million is set-aside for preservation. In comparison, the Metro Region is allocated \$4.0 million of which \$1.4 million is set aside for preservation. It is likely there will be more competition for 9% LIHTC in RD preservation projects in the Balance of State Region than in the Metro Region.



Changes in LIHTC policy directly influence which housing projects receive funding across the state. By following a comprehensive statewide housing plan with measurable goals, OHCS will be able to strategically adjust preservation set-asides and other LIHTC policies to reach preservation goals.

Increased gap funding could help expand use of 4% LIHTC

To help provide for more preservation projects, it is important for OHCS to take advantage of available funding sources and expand the use of the 4% LIHTC. Of a project’s total cost, 30% is funded with LIHTC equity, a minimum of 50% is required to be funded with tax-exempt private activity bond funds, and the remaining percentage is paid with developer contributions and gap funding, which is the remaining funding necessary to complete the project. The only limit to this funding source is the bond cap.



To encourage the development of projects, more gap funding needs to be identified and pursued. Although current funding streams provide some gap funding, stakeholders stated there are insufficient levels of gap funding to meet demand. This was a primary reason developers did not initiate more 4% LIHTC preservation projects. Another large barrier to program usage is that the program is not conducive to smaller projects.

The lack of gap funding also played a part in OHCS not taking advantage of available private activity bond authority. Between 2011 and 2015, OHCS only used 22% of the private activity bond authority available. As a result, OHCS did not take advantage of nearly \$1.7 billion in available bond monies that could help fund preservation projects. Given that these monies may not always be available, the state could be missing out on funding opportunities to preserve affordable housing.

Oregon falls behind other states when it comes to providing gap funding. Some states, like Vermont, Indiana and New Jersey, target preservation by setting money aside in trust funds. Washington State’s Housing Trust Fund at its height was \$200 million; but in more recent years has been \$70 million. In comparison, in 2016, the OHCS housing trust fund was about \$15 million.

Expanding the state housing tax credit program could help preservation efforts

The Oregon Affordable Housing Tax Credit Program was created in 1989 to provide Oregon tax credits to lenders of housing loans. The tax credits allow lenders to reduce the interest rates on loans for housing projects by as much as 4%. In most cases, property owners pass the savings they receive on their loans to their tenants in reduced rents. When paired with the 4% LIHTC program, the state tax credit program can increase feasibility of preservation projects with federal rent subsidies. The state tax credit program is a revolving fund with a limit of \$17 million; as owners repay their loans, credits become available for future awards.

OHCS staff reported the state tax credit program is a good vehicle for federal rent subsidy preservation, and stakeholders agree. Staff also stated that available program funds were not sufficient to meet the demand. The program is scheduled to sunset in 2020, but will be under legislative review in 2017. Continuing this program, potentially with more funding, could benefit preservation efforts.

Strategic planning is not sufficient



State law tasked OHCS with being the state leader in housing policy and serving as the central source of affordable housing data, training and technical information.

Through our review of the agency and comparisons to housing finance agencies in other states, we found OHCS is not achieving the expectations set out for them by the Legislature, public, stakeholders, and partners. We also found that OHCS needs to improve its strategic planning to better provide for affordable housing in the state.

Improved strategic planning critical to fulfilling agency priorities

Inadequate strategic planning results in unclear priorities, lack of vision for the future, and potentially, loss of opportunities to preserve affordable housing. Improved planning will help OHCS identify priorities for its limited resources, recognize success, detect problems, and respond with corrective action.

Housing finance agencies use strategic plans to set priorities, carry out comprehensive plans, allocate internal resources based on priorities, and guide staff in day-to-day decision-making. For example, in Minnesota, each section within the housing finance agency has a vision statement that ties back to the strategic plan, showing staff how their work ties into the larger vision and mission of the agency.

As part of the OHCS transition process in 2013 and 2014, management created an operations plan with strategic priorities, on which the agency reports they have made progress. However, the plan lacked many of the elements experts agree are essential to the strategic planning process. This

has led to an agency unable to clearly articulate strategic priorities or focus on highest priority work.

OHCS management identified five “imperatives” in the operations plan:

1. Implement an effective and integrated governance model;
2. Deliver remarkable service;
3. Increase leadership skills at all levels;
4. Implement a fiscally sustainable business model; and
5. Become a data and research driven agency.

While these are laudable goals, they are not specific and are difficult to measure. When OHCS management updated their plan, they added a sixth imperative. Like the other imperatives, it lacked specificity:

6. Develop and implement new programs.

Further, executive management was unable to provide documentation of key elements of a strategic planning process, such as an environmental scan. Environmental scanning is a vital element within the strategic planning process. It helps an organization identify and address internal strengths and weaknesses, while anticipating and planning for external threats and challenges such as social, economic, political and technological changes.

Some OHCS staff indicated they were unclear on the priorities, vision, or direction of the agency. Many felt leadership did not listen to concerns; others stated they were not informed about or included in the strategic planning process and were confused on how their work connected to the agency’s strategic plan.

Staff also voiced frustration about the lack of updates to the planning process. One staff member stated, “Sometimes it feels like we are stuck in things we decided 2-3 years ago. Things have changed since then, but we aren’t taking that into account.”

Along with staff, stakeholders agreed the agency did not clearly communicate its priorities.

We found examples of other state housing finance agencies that connect their statewide plan with strategic priorities to address challenges, including preservation. During strategic planning, Delaware’s housing agency found that significant funds to preserve federally subsidized housing were needed. It linked the physical condition of properties and cost of preservation to federal funds this money would leverage if allocated. As a result, the state Legislature approved a \$7.5 million bond bill for preservation.

Essential Elements of Successful Strategic Planning

- Documentation
 - Continuous and evolving
 - Environmental scan
 - Targeted strategies
 - Specific, measurable, and realistic goals
 - Action-oriented
 - Implementation plan
 - Evaluation plan
 - Clear mission and vision
 - Prioritization
 - Participatory
 - Effective communication
-



Strategic planning excluded staff and key stakeholders

Following the appointment of a new director and transition planning, the agency began a strategic planning process in 2014. Only the executive team, guided by consultants, was involved in creating a new mission and vision for the agency. Staff, the Housing Stability Council, and key external stakeholders were not included in these discussions. Research suggests this kind of top-down approach can lead to rigidity and inability to strategize appropriately within an evolving environment.

Harnessing staff knowledge and passion is a powerful tool the agency can use to engage in successful strategic planning. By not including staff in the strategic planning process, OHCS leadership missed a key opportunity to learn from and motivate staff and to boost morale, which is low according to our conversations with staff.

In addition to agency staff, the Housing Stability Council was not included in the strategic planning process. We were told they did not know the executive team was creating a new mission and vision until it was presented to them. Also excluded from the process was CAPO, the agency's partner in delivering homelessness assistance programs. Members of CAPO stated that during the transition planning process leading up to strategic planning, agency management was "unwilling" to articulate priorities or share strategies of how to accomplish shared goals.

Better data management needed for informed decision-making

Inadequate resources dedicated to data systems and data management resulted in OHCS not effectively using data to inform planning and decisions. This can affect program success, including the preservation of affordable housing.

Results from our survey and interviews with OHCS staff revealed two big challenges staff face—outdated IT systems and a general lack of data. These sentiments were also echoed in a recent OHCS annual customer service survey with stakeholders and partners citing concerns around data and decision-making. For example, one comment indicated OHCS has "premature and inaccurate publication of data" and there is a "lack of effort and funds to keep data systems current and high functioning."

The lack of complete and accurate data on the multifamily affordable housing portfolio kept us from completing planned work related to preservation. This included evaluating the effects of OHCS underwriting policies, as well as overall trends of properties in need of preservation.

Information technology resources have not kept pace with demand

In recent years, OHCS recognized the need for better data to improve decision-making. In a 2014 presentation to the Legislature, OHCS identified the lack of an integrated system as a cause of poor data. Efforts to move

"Improved systems, databases, and enough staff to manage these systems is key to understanding the effectiveness of the agency's work and making improvements."

-Respondent, 2016 OHCS Customer Service Survey

toward an integrated system began in 2015 and continued throughout our audit.

Additionally, OHCS expressed its intent to move toward data and research driven policy priorities and outcome measures in 2014. While this intent was included in an overall strategic plan, the plan did not include steps the agency would take to achieve this goal. Nor did it identify limitations, such as capacity, that might need to be addressed. Little tangible progress has been made on this initiative.

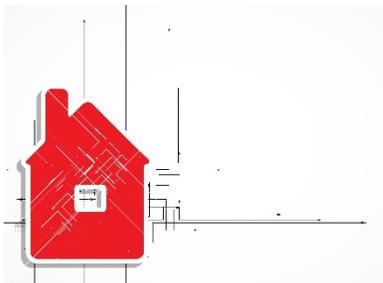
Staff capacity within the OHCS Information Technology (IT) unit has declined from 18 to 10 positions since the 2009-2011 biennium. OHCS management believes a handful of staff sought positions at other agencies due to concerns the agency would be dissolved. Some positions were simply not filled and others were eliminated, which could impede the agency's ability to address data issues. Management reported turnover and staffing constraints also impacted their efforts to integrate data systems.

Unreliable inventory and data silos contribute to data issues

The two IT systems within the OHCS Housing Finance Division, which are key to tracking multifamily affordable housing projects, are not integrated. As a result, OHCS is not able to gather and report historical information and trends on existing properties. In addition, the separate systems have contributed to an unreliable inventory of OHCS-funded housing projects.

Ideally, one data system should be used by both the Multifamily and the Asset Management and Compliance Sections to track the housing portfolio from application to asset monitoring. Currently, housing application information is entered into the agency's Information System for Housing (DISH). If a project is funded, it is recorded in Housing Development Software (HDS). The Asset Management and Compliance team uses HDS to monitor and inspect properties for the Multifamily housing portfolio. If the two systems were integrated, historical information and trends on properties and final loan figures could be compared to front end estimates to assist in developing underwriting guidelines for loan officers. This information could also help determine what financial underwriting factors might contribute to property deterioration or jeopardize long-term financial stability, as well as inform the development and maintenance of underwriting standards going forward.

During the audit, we requested a complete inventory of the OHCS multifamily housing portfolio but the agency could not provide consistent information. For example, we were told the number of properties in the OHCS portfolio was 987, and then later informed it was 1,289. The OHCS website indicates 1,243 funded properties. A presentation to the Housing Stability Council in March 2016 showed the OHCS portfolio included 1,343 properties valued at \$6 billion. Later we were told this amount may be inaccurate. According to the agency, part of the inventory problem was that there has not been a common understanding of what portfolio means.



Systems that are not integrated increase the risk for inaccuracies and the inability to track information from system to system. The unique identifier or number created to track projects from one system to another had not been consistently entered over time. At the completion of the audit, the agency was able to devote resources to reconcile data for the majority of projects recorded in the two systems, HDS to DISH. However, they were still working to ensure the HDS system information was complete and all properties that should be recorded are recorded.

Outdated data systems, cumbersome workarounds, and untracked performance indicators cause problems

The systems that OHCS uses to track properties were designed in the early 2000s. Over the last 10 years, cumbersome workarounds have evolved, including tracking information in separate spreadsheets by multiple individuals. The age of the systems and these workarounds make it difficult for staff to extract information; only a few staff have the long-term knowledge and expertise to do so.

For example, HDS does not have the ability to record affordability expiration dates, so information is tracked in a separate spreadsheet. These dates are important to asset management because they signal when a property may be at risk to convert to market rate. Tracking these dates enables the agency to identify and plan for upcoming preservation needs. When we reviewed the spreadsheet, we found many expiration dates were blank or missing. Project identification numbers needed to match expiration information back to the system of record were also not included.

There are various performance indicators and measures that, if tracked, could help OHCS measure its success and plan for the future. Information such as the number of applications by funding cycle versus the number of projects funded is an important measure to determine the level of need in the state. This comparison could also be used to determine if the agency is able to meet the demand through project funding.

Tracking the number of preservation projects funded by year and by geographic area would also help OHCS determine areas to target. We found this information was either tracked in a spreadsheet that did not agree to other systems, or was not tracked consistently. For example, the agency has a field to indicate if a project was a preservation project. Our review showed that the data was not consistently recorded and did not agree from spreadsheet to spreadsheet. Other important information such as length of time from application submission to funding, which would give good information on workload and capacity, was not tracked or used consistently.

Data entry into spreadsheets also resulted in time-consuming processes. For example, one staff enters information in DISH then enters the same information into separate spreadsheets. This dual entry is not efficient and increases the likelihood of errors and inconsistencies.

A lack of controls over data entry led to inconsistent entries across databases and spreadsheets. We noted differences in project naming conventions and differences in dates when housing developers received funding in multiple years. We also found numerous data errors, duplicate properties, and other missing or incomplete information.

Collection and analysis of data to guide decisions needs improvement

OHCS could improve on the collection and use of financial data from affordable housing projects placed in service. This data could highlight common characteristics of successful and unsuccessful properties and help identify best practices.

The Housing Development Center, a nonprofit organization, with help from Meyer Memorial Trust and funding from Chase Bank, compiled financial information on 140 affordable housing properties in Oregon with 5,967 rental units placed in service prior to 2012. One of the most important outcomes from this project was the high need for preservation funding and resources. This nonprofit will be working with developers in the housing industry to continue studying the need for preservation and strategies they can employ to improve performance. Additional key findings included:

- financing decisions affect long term project viability;
- 20% of properties were unable to cover expenses and debt in at least two of the three years analyzed; and
- some vulnerable properties could be refinanced to allow funding for repairs and improvements, but significant public investment will be necessary to preserve the portfolio.

Beginning in 2016, OHCS' Asset Management and Compliance Section began a financial risk assessment project to classify all properties within the OHCS portfolio as performing, troubled, or potentially troubled. Once this information is obtained and entered into the database, OHCS can use it to identify troubled properties. It can also determine common financial characteristics of troubled properties to help guide underwriting standards and policy decisions such as how properties can remain affordable for the 60 years affordability period.

Eliminating an award winning system leaves OHCS without important information

OHCS developed the Analysis of Income and Expense System in 2006 to track operating expenses on a project-by-project basis. OHCS used it to report information on project operating expenses by region and project type. In 2010, the National Council of State Housing Agencies gave OHCS a program excellence award for this system.



In 2012, the OHCS leadership discontinued the system and to date, it has not been replaced. As a result, loan officers have been unable to assess operating expenses during the underwriting process and asset management staff have not been able to determine whether properties are financially viable.

OHCS is hopeful a replacement system will provide staff support for underwriting decisions moving forward, as well as provide information developers appreciated.

Organizational challenges impede agency from addressing affordable housing

Much of our audit focused on OHCS' Multifamily Section within the Housing Finance Division. However, we identified organizational issues that cut across all sections of the agency, including lack of communication, unclear roles, inconsistent staffing levels, and inadequate policies and procedures. These areas need to be improved so that OHCS can successfully manage its programs, including preserving affordable housing in Oregon.

Management should demonstrate commitment to improving in these critical areas through leadership and effective communication with staff and stakeholders.

Tone at the top and internal communication can be improved

We found significant issues with both OHCS' tone at the top and internal communication. Both are influenced by leadership's operating style and management philosophy, among other things. More importantly, both are critical for the agency to successfully manage its priorities, which include preserving affordable housing.

Early on, we were told executive leadership's management style did not build trust. To gain a better understanding of the agency environment we conducted a workplace environment survey of agency staff. The survey included questions regarding the current work culture; 83% of staff responded to the survey.

During interviews and in the survey staff stated that executive leadership was top-down, reactionary, unsupportive, and lacked transparency. These things prevented executive management from building trust with staff. One

"Agency leadership should trust their experienced and dedicated staff more. Leaders have come and gone, but the workers have been there through thick and thin. Valuing the staff will in turn lead to better services to customers."

-Respondent, 2016 OHCS Customer Service survey

staff member stated staff used to be vocal and share their concerns, but are less so now because their suggestions were not acted on or taken seriously.

In addition, many staff indicated most executive managers are inaccessible or unapproachable, making internal communication a challenge. Some also stated that their expertise is disregarded, as executive leadership makes decisions in a vacuum without tapping into staff expertise and with little two-way communication. Internal communication among staff could also be improved. Only about half of staff who responded to our survey thought their co-workers shared job knowledge across work sections.

Further, some staff stated they do not always receive the necessary information they need to do their job and are often not involved in decisions impacting their day-to-day work. In the Multifamily Section, program staff stated that their input was not always sought for program development. For example, key staff responsible for implementing the new Local Innovation and Fast Track program, which is designed to fund projects that can quickly produce housing in high need areas, told us they were not consulted on its design. Also, responses to our survey showed a workplace with significant challenges where staff felt stressed and unsupported by executive management, especially staff in the Housing Finance Division.

Figure 1: OHCS Challenges with Internal Communication as Indicated in Audits Division 2016 Workplace Environment Survey

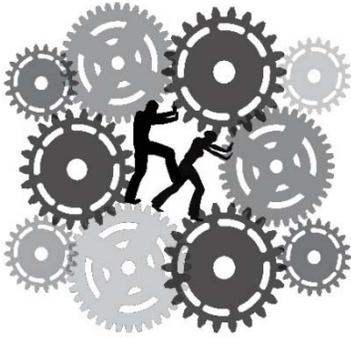
Workplace Environment Survey, Executive Team section	Housing Finance Staff Agreement	Agency Staff Agreement
Executive team is open and honest in communication	40%	53%
Executive team encourages staff to communicate suggestions for improvements	48%	60%
Staff in my workplace communicate openly and honestly to the Executive team	37%	41%
I receive information that will affect OHCS as a whole from the Executive team	43%	54%
Executive team understands my job well	19%	34%
Executive team is accessible to staff	32%	41%
Executive team cares about staff concerns	37%	57%
Executive team is aware of staff concerns	34%	43%

Decreased staff levels and increased workload stress staff

Although our audit focused on the agency’s Multifamily Section, we saw capacity issues throughout the agency, including the loss of institutional knowledge and experience. The current workload and capacity leaves little time for management and staff to analyze decision-making and data that could help improve administrative systems and policy.

Multifamily Section staff underwrite projects for affordable housing resources, review applications, and manage programs— all processes critical to preserving affordable housing. The section has experienced a loss

of institutional knowledge due to turnover and agency restructuring, and increased workloads.



Over the past five years, the number of Multifamily staff has remained relatively steady, but the workload has increased considerably. During interviews, staff said they struggle to keep up with the work and are burnt-out and tired. In our survey, 40% of Housing Finance staff, which includes Multifamily, reported their work related stress was too high. In addition, 37% reported they were assigned more work each week than they could reasonably accomplish. Less than half of Housing Finance staff thought their section had sufficient resources to do their job well and 67% thought they had the tools, such as technology and equipment, to do their job well. Despite this, 84% of Housing Finance staff reported they were proud to be a part of the agency.

The Multifamily Section's turnover rate increased dramatically since 2012, resulting in a complete turnover of the 4% LIHTC team, and about half of the 9% LIHTC Team. Though new staff have been added, there is a steep learning curve as they learn processes and become as efficient in their work as more seasoned staff.

Multifamily staff must score applications, underwrite and close projects selected for funding. As the number of funding opportunities and applications has increased, so has staff workload. In 2013, the agency moved to a new funding process. As a result, the agency went from one or two funding opportunities a year to eight in a single year, with individual applications, processes, and timelines for each funding stream.

As of July 2016, there were 71 funded projects in various stages; projects can take about two years from start to finish. Management expects the workload to continue increasing through the end of 2016 and into early 2017 as several more housing projects are funded.

To gauge the agency's ability to take on additional preservation efforts, an evaluation of workflow and resources is needed. One possible approach for evaluating workflow is Lean, which focuses on identifying and then implementing the most efficient, value-added processes. Having a better understanding of workflow and available resources will aid the agency and its Multifamily Section in identifying existing capacity for additional work, as well as areas where they may need additional staff or resources.



Outdated, absent, and weak policies and procedures hinder agency programs

We found some agency policies and procedures were absent, outdated, or weak. Policies and procedures are important to ensuring risks are mitigated and objectives are met.

Approximately half of the Housing Finance staff reported practices and procedures were not up-to-date. When we dug in deeper to understand the issue, we learned loan officers are struggling with outdated or undocumented procedures. For example, the desk manual for loan officers has not been updated in several years, which is problematic given the fast-paced nature of the changes within the agency. In addition, loan officers do not receive any training.

Underwriting staff also reported many practices and procedures in their department are not documented in policy, which can lead to inconsistency across loan officers' work. OHCS does not have a program manual for the 4% LIHTC program, but reports they are working to develop one.

There are also instances of policies that could be improved, such as the conflict of interest policy. The policy directs staff to bring actual or potential conflicts to their supervisor's attention in writing. However, we learned supervisors are not always aware of conflicts involving OHCS staff. For example, during the audit an employee also served as the board chair of a nonprofit organization that applied for funding from OHCS. When the organization did not receive the funding, the employee questioned another OHCS staff member as to why. The staff member felt uncomfortable discussing the information with their co-worker and reported the issue to their supervisor who had no knowledge or documentation of this person's potential conflict prior to the issue arising.

A more robust way to determine conflicts of interest at the agency would be to survey staff on an annual basis to document any actual or potential conflicts. It is impossible to avoid all conflicts of interest, but each instance should be documented and managed to ensure employee decisions are impartial and untainted by conflicts of interest.

Housing Stability Council unclear on role

Recent legislation transitioned the Housing Stability Council into a policy-setting board, setting the stage for the Council to play a bigger leadership role. Despite this legislation, there is lack of clarity about its role.

In addition, the communication between OHCS leadership and the Council could be improved. In general, Council members do not feel they receive information they need to make complex decisions in a timely manner.

While Council members are eager to be more involved and fulfill the new role, they do not feel the agency involves them in preliminary discussions around program and policy development. For instance, in 2016, Council

members were asked to approve the Manufactured Home Park NOFA application before they had the chance to discuss underlying policy.

Moving forward, the Council believes a fundamental discussion with agency leadership about its role would be beneficial.

Agency contracting policies and practices need improvement

OHCS does not have standardized or written contracting policies and procedures. Without clear policies and procedures outlining oversight responsibilities, contracts may not be vetted appropriately, deliverables may not be received, and contracts may extend beyond the agreed upon time and monetary limits.

We found that OHCS contracting is inconsistent both in administration and results. We also found little evidence that the agency monitors contracts to ensure deliverables are received.

OHCS has contracted with and overseen the contract with Neighborhood Partnerships, a nonprofit in Portland that has managed the successful Individual Development Account (IDAs) Initiative since 2003. The contract has been continuously renewed. It has never been put out to bid, which is contrary to standard contracting practices, though OHCS assured our team the contract will go to bid next year.

In another example, we found a consultant was hired in early 2013 to assist with the agency transition. The contract limit started at approximately \$150,000 but was amended four times extending the timeline and total dollar amount to \$428,000. According to the former director, the contractors' work products centered on organizational development as well as two staff surveys. It was not clear why the dollar amount was increased or whether all deliverables were ultimately received. Despite these questions, the agency hired the consultant again in 2015.

In a third example, OHCS hired a contractor in January 2016 and paid over \$6,000 to improve a customer service survey for external stakeholders and partners using "best practices and emerging research" regarding survey design. The goal was to achieve a higher response rate than in previous years. However, the response rate actually declined— only 155 out of 1,514 responded, a 10% response rate, compared to 13% in 2014 and 19% in 2011. Additionally, the contractor did not help agency staff analyze responses as outlined in the contract.

IDAs are matched savings accounts that build the financial management skills of qualifying Oregonians with lower incomes while they save towards a defined goal.

Recommendations

Addressing the following recommendations will take time and a coordinated approach.

We recommend Oregon Housing and Community Services management address the following four recommendations first, followed by those listed below.

- Lay the groundwork for improved tone at the top and internal communication by building an inclusive culture where communication, trust and transparency are embraced and management is accessible to staff.
- Strengthen organizational culture. Discuss the 2016 Workplace Environment survey results with staff and the Housing Stability Council, and address issues identified, paying special attention to internal communication and feedback mechanisms.
- Use a systematic approach to evaluate workflow and resources in the Multifamily Section. This includes assessing financial and administrative capacity to achieve the section's primary functions.
- Create a new single system of record to help manage properties. Consult with staff to determine data elements needed for a new IT system.

Preservation

- Build on the existing Consolidated Plan to develop a comprehensive state housing plan and ensure it includes:
 - information on market and housing inventory conditions;
 - an accurate inventory of all affordable housing in the state;
 - a needs assessment;
 - strategies to address need and housing condition;
 - analysis of all private, federal, state, and local government resources;
 - a plan for coordination of resources; and
 - an implementation plan that includes measurable goals with plans on how to achieve them.
- Strengthen partnerships with stakeholders involved in preservation, especially HUD and RD.
- Develop a clear channel for external communication to and from partners and stakeholders, especially for the Housing Finance Division.
- Consider dedicating staff to monitor and coordinate the state's preservation efforts to ensure efforts are consistent and focused.
- Consider coordinating application funding and timelines with federal, state, and local funders.
- More clearly articulate preservation strategies and priorities in the LIHTC Qualified Allocation Plan.
- Consider working with the Legislature to increase gap funding to use with the LIHTC 4% program.

- Consider working with the Legislature to expand the Oregon Affordable Housing Tax Credit program.

Strategic Planning

- Engage in long-term, comprehensive strategic planning to create a vision for affordable housing and set the stage for the agency to provide leadership on housing issues. Develop a plan with input from all levels of the organization that incorporates the agency's mission, performance metrics, and goals specific to each section of the agency.

Data Management

- Review current IT capacity and incorporate strategies to address capacity needs and issues into the formal strategic plan.
- Define portfolio and identify properties within it.
- Identify and collect data elements to inform decision-making for underwriting and asset management.
- Consider developing systems to track operating expenses on an ongoing basis to provide a foundation for underwriting standards.
- Continue to collect property information to develop a single reliable source of all affordable properties in the state.

Organizational Challenges

- Consider filling the internal auditor position to help conduct risk assessments and to ensure strong internal controls are in place.
- Improve communication and transparency with the Housing Stability Council.
- Involve staff and incorporate their feedback in decisions that impact their work.
- Work with the Legislature and Housing Stability Council to clarify in statute the roles of the OHCS director and Housing Stability Council in leading the agency.
- Update and document processes for underwriting, including formal written policies and procedures, and guidance for loan officers.
- Strengthen the conflict of interest policy and ensure it is followed.
- Improve and document processes for contracting, including formal written policies and procedures.
- Ensure contractors' performance is adequately monitored and deliverables are received.

We recommend the Housing Stability Council:

- Work with the agency and Legislature to clarify its role.
- Communicate the Council's training and information needs to agency management.

Objectives, Scope and Methodology

The objective of this audit was to determine how OHCS could best preserve affordable housing in Oregon. We focused our efforts on the agency's Multifamily Section within the Housing Finance Division and completed our fieldwork in September 2016.

The lack of complete and accurate data on the multifamily affordable housing portfolio kept us from completing some planned work related to preservation. This included evaluating the effects of OHCS underwriting policies as well as overall trends of properties in need of preservation.

To address our audit objective, we reviewed applicable state laws, and rules as they relate to multifamily housing and preservation of affordable housing. We reviewed the agency's program manuals, policies and procedures, contracts, staff surveys, external customer surveys, and planning documents. We also reviewed literature on affordable housing preservation, data management, strategic planning, and internal control. To further identify promising practices related to affordable housing preservation, we developed and administered a state Housing Finance Agency questionnaire to six states, and conducted follow-up interviews.

We reviewed documents prepared by the Legislative Fiscal Office to understand historical context for OHCS programs and its budgets.

We conducted interviews with nearly 40 current or former OHCS staff. We also spoke with over 30 stakeholder groups. Stakeholders included housing authorities or nonprofits involved in developing housing and delivering services to tenants of affordable housing; for-profit and nonprofit affordable housing developers; local governments involved in developing affordable housing; and other government officials. We also attended a meeting of a housing authority's resident advisory committee. To assess staff thoughts and feelings about their work experience, we conducted a workplace environment survey, which was sent to 116 staff. Ninety-six staff completed the survey, an 83% response rate. The survey had 68 questions we developed and 10 additional questions OHCS requested be included.

We toured a property nearing the end of its first 15 years of affordability as well as a property over a hundred years old that had recently been rehabilitated with its federal subsidies preserved.

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

Auditors from our office, who were not involved with the audit, reviewed our report for accuracy, checking facts and conclusions against our supporting evidence.

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Oregon

Governor Kate Brown

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November 29, 2016

Mary Wenger, Interim Director
Oregon Audits Division
255 Capitol Street NE, Suite 500
Salem OR 97310

Dear Ms. Wenger:

First, let me acknowledge all the hard work done by your Audit Division team to prepare this audit of affordable housing preservation programs here at Oregon Housing and Community Services. It has been a long process but I think the work done in this audit will help move our agency forward and I thank your team for their effort.

Second, let me say that many of the issues identified in the audit reaffirm what we already know. Oregon Housing and Community Services has a lot of work to do in the areas of data management, development of a statewide housing plan and strategic planning. Maybe most importantly, the identified problems with communication and transparency between the executive team and the rest of the agency require immediate attention. I can assure you we are taking these recommendations very seriously and are committed to correcting the identified areas of concern.

The good news is, in the areas involving data management and integrity, the agency was aware of those problems and began addressing them even before the audit began. Data issues were identified in 2014 and we started the process of upgrading and improving the system from that point. Ultimately we hope to have a new Multifamily Finance data system in place by the end of 2017 that will allow us to house all the information needed to guide our decisions and investments and streamline our system.

In much the same way, the agency recognized the need for the Statewide Housing Plan and began work on developing that plan in 2015. It is not lost on anyone at the agency that Oregon faces a housing crisis and that a plan that will use data and research to guide the investment of our scarce housing dollars is top priority. This will be the first housing plan the agency has produced in years and we are excited to create something that will guide Oregon housing decisions and investments for years to come.



Lastly, before the point-by-point response to the recommendations provided in the audit I also know it is important to recognize the organizational challenges OHCS currently faces. While I am new in my role as Director of OHCS I have come to quickly understand the need to address these critical issues. Transparency in how we do our work at the executive level and the ability for all staff to see themselves in the work we do is crucial to this agency's success. I know everyone here, including executive staff, understand and support this approach but clearly we have work to do. I am committed to that work and we are starting fresh to involve staff in the formation of strategic goals for 2017 that I believe will set a new tone and level of engagement with all staff. I very much look forward to that work.

Recommendations

Recommendation: Lay the groundwork for improved tone at the top and internal communication by building an inclusive culture where communication, trust and transparency are embraced and management is accessible to staff.

Response: As the new Director I am taking immediate action to build an inclusive culture by making myself available to staff with a regularly scheduled coffee, opening Housing Stability Council meetings to all staff, providing my notes from leadership team meetings to all staff and asking for Assistant Directors to include staff in development of 2017 strategic goals.

Recommendation: Strengthen organizational culture. Discuss the 2016 Workplace Environment survey results with staff and the Housing Stability Council, and address issues identified, paying special attention to internal communication and feedback mechanisms.

Response: I am holding an all staff meeting on December 1st to present the results of the audit and the survey and asking for small group breakouts with all staff to develop ideas on improving our culture and communication. The goal is to develop and deliver on a comprehensive platform of action items to build employee engagement, develop leadership and improve communication.

Recommendation: Use a systematic approach to evaluate workflow and resources in the Multifamily Section. This includes assessing financial and administrative capacity to achieve the section's primary functions.

Response: The Multifamily Finance section faces a significant workload that creates challenges across the agency. The addition of new programs, and a pronounced need for affordable rental housing development, have strained existing staff in recent years. The agency has recently made some staffing changes and hired a new manager to help alleviate this crunch, but we believe additional staffing is warranted. To address that need OHCS requested positions related to LIFT and underwriting capacity in our Agency Request Budget.

While we continue to evaluate our staffing needs, we are also working to streamline and modernize our business practices to allow staff to focus their time where it is most

urgently needed – underwriting complex affordable housing transactions and developing strategies for increasing housing production. This includes engaging staff and stakeholders in an ad hoc work group to discuss barriers and improvements that can be made to the 4% Low Income Housing Tax Credit program, which we believe has great potential to expand use in Oregon as a tool for housing development and especially for affordable housing preservation. We are also implementing a new data system which we believe will greatly increase productivity and decrease workload through electronic application processing and electronic file management.

Recommendation: Create a new single system of record to help manage properties. Consult with staff to determine data elements needed for a new IT system.

Response: We are in the process of implementing a Multifamily data-systems modernization project. As noted above, the need for this is not new to OHCS and we are engaged with the State CIO's office to provide project oversight. The end product will be a single integrated data system to house all information needed to make strategic planning and investment decisions regarding multifamily housing resources. This will also help to streamline our Multifamily underwriting, and asset management and compliance processes that will create a better user experience for staff and our customers.

Preservation

Recommendation: Build on the existing Consolidated Plan to develop a comprehensive state housing plan and ensure it includes:

- information on market and housing inventory conditions;
- an accurate inventory of all affordable housing in the state;
- a needs assessment;
- strategies to address need and housing condition;
- analysis of all private, federal, state, and local government resources;
- a plan for coordination of resources; and
- an implementation plan that includes measurable goals with plans on how to achieve them.

Response: Preservation efforts are critical in the continuing effort to address the shortage of affordable housing in Oregon. We are building that work into our Statewide Housing Plan. Staff has been hard at work in 2016 to initiate work on the Housing Plan, including robust work on housing needs and regional profiles. We will be issuing a Request For Quotation within the next two months to bring in additional help to create a plan that will include robust stakeholder engagement across the state help guide these investments. We are also reaching out and researching national best practices so we can align programs with successful efforts that have been identified in other states.

Recommendation: Strengthen partnerships with stakeholders involved in preservation, especially HUD and RD.

Response: OHCS will be building on the successful work of the preservation workgroup discussed in the audit document to identify needs and resources for federal preservation and local preservation efforts. My previous experience is in the federal system and I have particular expertise in the arena of affordable housing preservation. I look forward to strengthening relationships with our federal partners to improve these efforts.

Recommendation: Develop a clear channel for external communication to and from partners and stakeholders, especially for the Housing Finance Division.

Response: We very much value our partners and the work they do to provide housing and critical services to needy Oregonians. We are developing a strategy for our Housing Finance division to more regularly communicate and engage with stakeholders to help address this issue including regular informational calls. We are also going to attend regular meetings of our stakeholder groups and I will be sending out a Director's message on a regular basis to help support the external communication work. We will continue to improve our customer service surveys as well to measure our progress.

Recommendation: Consider dedicating staff to monitor and coordinate the state's preservation efforts to ensure efforts are consistent and focused.

Response: Although our staffing levels are thin, we will certainly be working to implement this recommendation. We will also include this as part of our strategic planning goals we develop for the future.

Recommendation: Consider coordinating application funding and timelines with federal, state, and local funders.

Response: We will certainly take this recommendation under advisement as we understand that coordinated timelines are beneficial to our partners.

Recommendation: More clearly articulate preservation strategies and priorities in the LIHTC Qualified Allocation Plan.

Response: We certainly agree and will be looking toward the Statewide Housing Plan and OHCS Strategic Planning efforts to develop strategies and priorities specifically for the preservation of existing affordable housing. Once direction has been adopted the QAP will be updated to incorporate appropriate implementation strategies and priorities.

Recommendation: Consider working with the Legislature to increase gap funding to use with the LIHTC 4% program.

Response: We certainly agree. OHCS has been pleased to receive gap funding from the Legislature in prior years, and as of this writing we are in the midst of a Notice of Funding Availability making \$5 million available in gap financing for affordable housing preservation for use with the 4% LIHTC program. In our Agency Requested Budget, we

requested \$10 million in lottery backed bonds to be utilized for gap funding for multiple purposes, preservation being one of those. If approved, this gap funding would allow us to preserve an estimated 200 homes. We appreciate the examples provided in the audit from other states and will also be reaching out to other state housing agencies to learn of additional best practices.

Recommendation: Consider working with the Legislature to expand the Oregon Affordable Housing Tax Credit program.

Response: We would be happy to work with the legislature to discuss the potential for expansion of the OAHTC.

Strategic Planning

Recommendation: Engage in long-term, comprehensive strategic planning to create a vision for affordable housing and set the stage for the agency to provide leadership on housing issues. Develop a plan with input from all levels of the organization that incorporates the agency's mission, performance metrics, and goals specific to each section of the agency.

Response: As noted above in the letter, OHCS has been in the process of developing a Statewide Housing Plan as required by statute and we are excited that this plan will use data and research to guide the agency and the Housing Stability Council in their efforts to address Oregon's housing crisis. We are also going to be developing annual measurable goals for the agency and the calendar year 2017 goals are already being considered and shaped. In 2017 leadership will also be engaging the Agency, from staff to the members of the Housing Stability Council, in the development of a five year strategic plan that will guide the work of the Agency. The plan will include clear annual goals and performance metrics and provide a framework for reporting the Agency's outcomes on an annual basis.

Data Management

Recommendation: Review current IT capacity and incorporate strategies to address capacity needs and issues into the formal strategic plan.

Response: We agree with this recommendation and have actively worked to address this need. Actions taken include analyzing gaps in capacity, creating business cases to identify options to address the gaps, adding temporary resources when available, and requesting requisite resources through the budget process. We will continue to monitor this closely to ensure the resources available help inform and align with the strategic plan.

Recommendation: Define portfolio and identify properties within it.

Response: We agree with this recommendation and are taking steps to address this through the data systems modernization project. The updated data system will contain a formal

data dictionary, naming conventions, and system controls to ensure common understandings of data elements.

Recommendation: Identify and collect data elements to inform decision-making for underwriting and asset management.

Response: We agree with this recommendation and are ensuring completeness and accuracy of these elements prior to migration of the data into the new data system.

Recommendation: Consider developing systems to track operating expenses on an ongoing basis to provide a foundation for underwriting standards.

Response: We agree with this recommendation and are currently populating this information in the Asset Management module in our current system of record, HDS. This information should be useable in the next 4-6 months. This functionality will also be a required element in the Request for Proposal to procure an integrated data system.

Recommendation: Continue to collect property information to develop a single reliable source of all affordable properties in the state.

Response: We agree with this recommendation and have been engaged with a workgroup since the beginning of 2016 to ensure all data sources are accounted for and the data included is accurate and reliable. OHCS also requested staffing resources in its Agency Request Budget to provide the capacity needed to establish and maintain a robust affordable housing inventory for the State

Organizational Challenges

Recommendation: Consider filling the internal auditor position to help conduct risk assessments and to ensure strong internal controls are in place.

Response: We agree with the need for a risk assessment and strong internal controls. OHCS has been exempt from internal audit requirements since 2013 and that exemption ends in fiscal year 2017. We will ensure a risk assessment is completed as part of the internal audit work in 2017, and meanwhile are actively working to ensure strong internal controls are executed.

Recommendation: Improve communication and transparency with the Housing Stability Council.

Response: This is an important issue and we are taking immediate action with a council retreat tentatively scheduled for January 2017 to develop better communication and transparency with the council. The retreat will include discussion about the role of the new council going forward, and also a discussion of training or information needed to better equip Council members to perform their roles on the Council.

Recommendation: Involve staff and incorporate their feedback in decisions that impact their work.

Response: Our staff has tremendous experience, energy and ideas for how to move the agency forward. We will be developing a comprehensive employee engagement platform and including this work in our strategic plans.

Recommendation: Work with the Legislature and Housing Stability Council to clarify in statute the roles of the OHCS director and Housing Stability Council in leading the agency.

Response: We recognize the unclear direction that statute creates in terms of the work of the Housing Stability Council. We will be working with our legal counsel and the Housing Stability Council to see what may need to be done to correct this and better define the work and role of the Housing Stability Council.

Recommendation: Update and document processes for underwriting, including formal written policies and procedures, and guidance for loan officers.

Response: We agree this is critical. The data systems work will inform this and Multifamily staff will create written procedures as part of its continuous process improvement work.

Recommendation: Strengthen the conflict of interest policy and ensure it is followed.

Response: We are bringing in the Ethics Commission as part of our training for the Housing Stability Council and will also be sharing that training with appropriate staff.

Recommendation: Improve and document processes for contracting, including formal written policies and procedures.

Response: We agree with this recommendation and have already completed and adopted a number of formal policies and procedures to guide procurement and contracting work. We have identified remaining policies and procedures to develop and have created a work plan to ensure they are adopted by the middle of 2017.

Recommendation: Ensure contractors' performance is adequately monitored and deliverables are received.

Response: We agree with this recommendation and will incorporate performance monitoring requirements as part of the policies and procedure mentioned above. Additionally we intend of providing education and training in alignment with requirements under HB2375 to ensure procurement staff and contract administrators understand their roles and responsibilities related to performance monitoring of contractors.

We recommend the Housing Stability Council:

Recommendation: Work with the agency and Legislature to clarify its role.

Response: The Housing Stability Council members agree with this recommendation and will be working with myself, the executive team and staff to implement.

Recommendation: Communicate the Council's training and information needs to agency management.

Response: Council members agree and this will be part of the regular communication between the agency and the council.

I hope that the responses and plan for implementation outlined above are received well by you and the audit team. Again, this audit provides valuable information for OHCS leadership and staff as we move forward into a very ambitious agenda. We know the housing crisis is not going away in the near future.

I would like to end our response with some examples of the good work the agency has done even during a very difficult transition effort and through changes in leadership. In 2015 OHCS funded 1,549 units of affordable housing, created 368 loans for first-time homebuyers through our Oregon Bond Loan program, and helped 2,252 homeowners avoid foreclosure through our Mortgage Payment Assistance program. Our Individual Development Account program is helping approximately 3,400 Oregonians save for future investments like education and homeownership. The agency has also provided homeless funds to over 15,000 families in need of assistance and helped over 81,000 low-income families in need of energy bill payment assistance.

As you can see, we have been hard at work and we are excited about our work ahead.

Sincerely,

A handwritten signature in black ink, appearing to read 'MS', with a long horizontal line extending to the right.

Margaret Solle Salazar

About the Secretary of State Audits Division

The Oregon Constitution provides that the Secretary of State shall be, by virtue of her office, Auditor of Public Accounts. The Audits Division exists to carry out this duty. The division reports to the elected Secretary of State and is independent of other agencies within the Executive, Legislative, and Judicial branches of Oregon government. The division is authorized to audit all state officers, agencies, boards, and commissions and oversees audits and financial reporting for local governments.

Audit Team

William K. Garber, CFGM, MPA, Deputy Director

Sandra K. Hilton, CPA, Audit Manager

Jamie Ralls, ACDA, CFE, Principal Auditor

Rebecca Brinkley, MPA, Staff Auditor

Danielle Moreau, MPA, Staff Auditor

This report, a public record, is intended to promote the best possible management of public resources. Copies may be obtained from:

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phone: 503-986-2255

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255 Capitol Street NE, Suite 500
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The courtesies and cooperation extended by officials and staff of Oregon Housing and Community Services during the course of this audit were commendable and sincerely appreciated.

Office of the Secretary of State

Jeanne. P. Atkins
Secretary of State

Robert Taylor
Deputy Secretary of State



Audits Division

Mary Wenger
Interim Director

255 Capitol St. NE, Suite 500
Salem, OR 97310

(503) 986-2255

February 29, 2016

Margaret Van Vliet, Director
Oregon Housing and Community Services Department
725 Summer Street NE, Suite B
Salem, OR 97301-1266

Dear Ms. Van Vliet:

We have completed audit work of the following selected federal program at the Oregon Housing and Community Services Department (department) for the year ended June 30, 2015.

<u>CFDA Number</u>	<u>Program Name</u>	<u>Audit Amount</u>
93.568	Low-Income Home Energy Assistance (LIHEAP)	\$ 33,605,176

This audit work was not a comprehensive audit of your federal program. We performed this federal compliance audit as part of our annual Statewide Single Audit. The Single Audit is a very specific and discrete set of tests to determine compliance with federal funding requirements, and does not conclude on general efficiency, effectiveness, or state-specific compliance issues. The Office of Management and Budget (OMB) Circular A-133 identifies internal control and compliance requirements for federal programs. Auditors review and test internal controls for all federal programs selected for audit and perform specific audit procedures only for those compliance requirements that are direct and material to the federal program under audit. For the year ended June 30, 2015, we determined whether the department substantially complied with the following compliance requirements relevant to the federal program.

Compliance Requirement	General Summary of Audit Procedures Performed
Cash Management	Confirmed program costs were paid for before federal reimbursement was requested, or federal cash drawn was for an immediate need.
Period of Performance	Determined whether federal funds were used only during the authorized period of performance.
Reporting	Verified the department submitted financial and performance reports to the federal government in accordance with the grant agreement and that those financial reports were supported by the accounting records.

Compliance Requirement	General Summary of Audit Procedures Performed
Subrecipient Monitoring	Determined whether the pass-through entity monitored subrecipient activities to provide reasonable assurance that the subrecipient administers federal awards in compliance with federal requirements.

Noncompliance

Noncompliance is a failure to follow compliance requirements, or a violation of prohibitions included in compliance requirements, that are applicable to a federal program. As described in the “Audit Findings and Recommendations” section, we identified noncompliance with federal requirements which is required to be reported in accordance with OMB Circular A-133.

Internal Control Over Compliance

Department management is responsible for establishing and maintaining effective internal control over compliance with program requirements. In planning and performing our audit, we considered the department’s internal control over compliance with requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on the department’s compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the department’s internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described above and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. As discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses.

Audit Findings and Recommendations

Improve Reviews of Subrecipients

Federal Awarding Agency: U.S. Department of Health and Human Services
Program Title and CFDA Number: Low-Income Home Energy Assistance, CFDA 93.568
Federal Award Numbers and Year: 2015G992201; 2015, 2015G992205; 2015,
2015G992212; 2015, 2014G992201; 2014,
2014G995623; 2014
Compliance Requirement: Subrecipient Monitoring
Type of Finding: Material Weakness, Noncompliance

Federal regulations require the department, as a recipient of federal awards, to monitor the activities of subrecipients to ensure that federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements. For the LIHEAP program, this includes monitoring subrecipients to ensure:

- Program funds are used for certain allowable activities;
- Specified “earmarking” limits are not exceeded; and
- Subrecipient cost allocation plans are in compliance with applicable cost principles.

We found the department does not have adequate controls to ensure only costs for allowable activities are reimbursed with federal funds; limitations are not exceeded; and ensure subrecipients follow general cost principles, including gaining assurances that expenditures charged to federal programs are reasonable, equitably distributed, and adequately documented.

This has been an ongoing finding since fiscal year 2012 due to a lack of adequate resources dedicated by the department to develop and maintain adequate controls. The department has been in the process of updating its fiscal monitoring controls but has yet to fully implement changes to ensure compliance with program requirements.

We recommend department management complete and implement an adequate fiscal monitoring process to ensure federal reimbursements are for allowable program activities, subrecipient cost allocation plans are sufficiently reviewed to determine whether the plans are in compliance with applicable cost principles, and required limitations are not exceeded.

Strengthen Controls Over Cash Management

Federal Awarding Agency: U.S. Department of Health and Human Services
Program Title and CFDA Number: Low-Income Home Energy Assistance, CFDA 93.568
Federal Award Numbers and Year: 2015G992201; 2015, 2015G992205; 2015,
2015G992212; 2015, 2014G992201; 2014,
2014G995623; 2014
Compliance Requirement: Cash Management
Type of Finding: Material Weakness, Noncompliance

Federal regulations require program costs be paid with entity funds before reimbursement is requested from the federal government. The exception to the cost reimbursement basis is the

advancement of federal monies to meet immediate cash needs. When awards provide for advance payments, recipients must follow procedures to minimize the time elapsing between the transfer of funds from the U.S. Treasury and disbursement by the recipient with similar procedures established for subrecipients. These regulations include expectations for the department to monitor cash drawdowns by subrecipients to ensure subrecipients conform substantially to the same standards of timing and amounts that apply to the department.

We found the department does not have adequate controls to ensure funds are provided as reimbursement of costs already paid by the subrecipient or that a minimal lapse of time occurred between the advancement to and disbursement of funds by subrecipients. This has been an ongoing finding since fiscal year 2010 due to a lack of adequate resources dedicated by the department to develop and maintain an adequate control process. The department has been in the process of updating its reviews of subrecipient requests for funds but has yet to fully implement changes to ensure compliance with cash management requirements.

We recommend department management complete and implement adequate controls to ensure subrecipient requests for funds are in compliance with federal cash management requirements.

Prior Year Findings

In the prior fiscal years, we reported noncompliance and internal control findings in the Statewide Single Audit Report related to LIHEAP. For the fiscal-year ended June 30, 2014; see Secretary of State audit report number 2015-05, and for the fiscal year ended June 30, 2013; see Secretary of State audit report number 2014-09.

During fiscal year 2015, the department continued to develop plans for addressing these findings. The last two years of prior findings listed below will be reported in the Statewide Single Audit Report for the fiscal year ended June 30, 2015 with a status of partial corrective action taken.

Finding Title	Prior Year Finding No.
Review of Subrecipient Costs for Allowability Should be Improved	2013-046
Strengthen Controls Over Cash Management	2013-047
Improve Controls Over Subrecipient Cost Allocation Plans	2013-048
Improve Reviews of Subrecipients	2014-036
Improve Reviews of Subrecipient Allocated Costs	2014-037
Strengthen Controls Over Cash Management	2014-038

The audit findings and recommendations above, along with your responses, will be included in our Statewide Single Audit Report for the fiscal year ended June 30, 2015. Including your responses satisfies the federal requirement that management prepare a Corrective Action Plan covering all reported audit findings. Satisfying the federal requirement in this manner,

Margaret Van Vliet, Director
Oregon Housing and Community Services Department
Page 5

however, can only be accomplished if the response to each material weakness includes the information specified by the federal requirement, and only if the responses are received in time to be included in the audit report. The following information is required for the each response:

- 1) Your agreement or disagreement with the finding. If you do not agree with an audit finding or believe corrective action is not required, include in your response an explanation and specific reasons for your position.
- 2) The corrective action planned.
- 3) The anticipated completion date.
- 4) The name(s) of the contact person(s) responsible for corrective action.

Please provide a response to us by March 7, 2016 and provide Rob Hamilton, Statewide Accounting and Reporting Services (SARS) Manager, a copy of your Corrective Action Plan.

The purpose of this communication is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this communication is not suitable for any other purpose.

We appreciate your staff's assistance and cooperation during this audit. Should you have any questions, please contact Wendy Hewitt, Principal Auditor or Julianne Kennedy, Audit Manager at (503) 986-2255.

Sincerely,

Office of the Secretary of State, Audits Division

cc: Caleb Yant, CFO
Claire Seguin, Assistant Director of Housing Stabilization
Sandra Flickinger, Financial Services Section Manager
Tim Zimmer, Energy and Weatherization Section Manager
George Naughton, Interim Director, Department of Administrative Services



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November 29, 2016

Mary Wenger, Interim Director
Oregon Audits Division
255 Capitol Street NE, Suite 500
Salem OR 97310

Dear Ms. Wenger:

First, let me acknowledge all the hard work done by your Audit Division team to prepare this audit of affordable housing preservation programs here at Oregon Housing and Community Services. It has been a long process but I think the work done in this audit will help move our agency forward and I thank your team for their effort.

Second, let me say that many of the issues identified in the audit reaffirm what we already know. Oregon Housing and Community Services has a lot of work to do in the areas of data management, development of a statewide housing plan and strategic planning. Maybe most importantly, the identified problems with communication and transparency between the executive team and the rest of the agency require immediate attention. I can assure you we are taking these recommendations very seriously and are committed to correcting the identified areas of concern.

The good news is, in the areas involving data management and integrity, the agency was aware of those problems and began addressing them even before the audit began. Data issues were identified in 2014 and we started the process of upgrading and improving the system from that point. Ultimately we hope to have a new Multifamily Finance data system in place by the end of 2017 that will allow us to house all the information needed to guide our decisions and investments and streamline our system.

In much the same way, the agency recognized the need for the Statewide Housing Plan and began work on developing that plan in 2015. It is not lost on anyone at the agency that Oregon faces a housing crisis and that a plan that will use data and research to guide the investment of our scarce housing dollars is top priority. This will be the first housing plan the agency has produced in years and we are excited to create something that will guide Oregon housing decisions and investments for years to come.



Lastly, before the point-by-point response to the recommendations provided in the audit I also know it is important to recognize the organizational challenges OHCS currently faces. While I am new in my role as Director of OHCS I have come to quickly understand the need to address these critical issues. Transparency in how we do our work at the executive level and the ability for all staff to see themselves in the work we do is crucial to this agency's success. I know everyone here, including executive staff, understand and support this approach but clearly we have work to do. I am committed to that work and we are starting fresh to involve staff in the formation of strategic goals for 2017 that I believe will set a new tone and level of engagement with all staff. I very much look forward to that work.

Recommendations

Recommendation: Lay the groundwork for improved tone at the top and internal communication by building an inclusive culture where communication, trust and transparency are embraced and management is accessible to staff.

Response: As the new Director I am taking immediate action to build an inclusive culture by making myself available to staff with a regularly scheduled coffee, opening Housing Stability Council meetings to all staff, providing my notes from leadership team meetings to all staff and asking for Assistant Directors to include staff in development of 2017 strategic goals.

Recommendation: Strengthen organizational culture. Discuss the 2016 Workplace Environment survey results with staff and the Housing Stability Council, and address issues identified, paying special attention to internal communication and feedback mechanisms.

Response: I am holding an all staff meeting on December 1st to present the results of the audit and the survey and asking for small group breakouts with all staff to develop ideas on improving our culture and communication. The goal is to develop and deliver on a comprehensive platform of action items to build employee engagement, develop leadership and improve communication.

Recommendation: Use a systematic approach to evaluate workflow and resources in the Multifamily Section. This includes assessing financial and administrative capacity to achieve the section's primary functions.

Response: The Multifamily Finance section faces a significant workload that creates challenges across the agency. The addition of new programs, and a pronounced need for affordable rental housing development, have strained existing staff in recent years. The agency has recently made some staffing changes and hired a new manager to help alleviate this crunch, but we believe additional staffing is warranted. To address that need OHCS requested positions related to LIFT and underwriting capacity in our Agency Request Budget.

While we continue to evaluate our staffing needs, we are also working to streamline and modernize our business practices to allow staff to focus their time where it is most

urgently needed – underwriting complex affordable housing transactions and developing strategies for increasing housing production. This includes engaging staff and stakeholders in an ad hoc work group to discuss barriers and improvements that can be made to the 4% Low Income Housing Tax Credit program, which we believe has great potential to expand use in Oregon as a tool for housing development and especially for affordable housing preservation. We are also implementing a new data system which we believe will greatly increase productivity and decrease workload through electronic application processing and electronic file management.

Recommendation: Create a new single system of record to help manage properties. Consult with staff to determine data elements needed for a new IT system.

Response: We are in the process of implementing a Multifamily data-systems modernization project. As noted above, the need for this is not new to OHCS and we are engaged with the State CIO's office to provide project oversight. The end product will be a single integrated data system to house all information needed to make strategic planning and investment decisions regarding multifamily housing resources. This will also help to streamline our Multifamily underwriting, and asset management and compliance processes that will create a better user experience for staff and our customers.

Preservation

Recommendation: Build on the existing Consolidated Plan to develop a comprehensive state housing plan and ensure it includes:

- information on market and housing inventory conditions;
- an accurate inventory of all affordable housing in the state;
- a needs assessment;
- strategies to address need and housing condition;
- analysis of all private, federal, state, and local government resources;
- a plan for coordination of resources; and
- an implementation plan that includes measurable goals with plans on how to achieve them.

Response: Preservation efforts are critical in the continuing effort to address the shortage of affordable housing in Oregon. We are building that work into our Statewide Housing Plan. Staff has been hard at work in 2016 to initiate work on the Housing Plan, including robust work on housing needs and regional profiles. We will be issuing a Request For Quotation within the next two months to bring in additional help to create a plan that will include robust stakeholder engagement across the state help guide these investments. We are also reaching out and researching national best practices so we can align programs with successful efforts that have been identified in other states.

Recommendation: Strengthen partnerships with stakeholders involved in preservation, especially HUD and RD.

Response: OHCS will be building on the successful work of the preservation workgroup discussed in the audit document to identify needs and resources for federal preservation and local preservation efforts. My previous experience is in the federal system and I have particular expertise in the arena of affordable housing preservation. I look forward to strengthening relationships with our federal partners to improve these efforts.

Recommendation: Develop a clear channel for external communication to and from partners and stakeholders, especially for the Housing Finance Division.

Response: We very much value our partners and the work they do to provide housing and critical services to needy Oregonians. We are developing a strategy for our Housing Finance division to more regularly communicate and engage with stakeholders to help address this issue including regular informational calls. We are also going to attend regular meetings of our stakeholder groups and I will be sending out a Director's message on a regular basis to help support the external communication work. We will continue to improve our customer service surveys as well to measure our progress.

Recommendation: Consider dedicating staff to monitor and coordinate the state's preservation efforts to ensure efforts are consistent and focused.

Response: Although our staffing levels are thin, we will certainly be working to implement this recommendation. We will also include this as part of our strategic planning goals we develop for the future.

Recommendation: Consider coordinating application funding and timelines with federal, state, and local funders.

Response: We will certainly take this recommendation under advisement as we understand that coordinated timelines are beneficial to our partners.

Recommendation: More clearly articulate preservation strategies and priorities in the LIHTC Qualified Allocation Plan.

Response: We certainly agree and will be looking toward the Statewide Housing Plan and OHCS Strategic Planning efforts to develop strategies and priorities specifically for the preservation of existing affordable housing. Once direction has been adopted the QAP will be updated to incorporate appropriate implementation strategies and priorities.

Recommendation: Consider working with the Legislature to increase gap funding to use with the LIHTC 4% program.

Response: We certainly agree. OHCS has been pleased to receive gap funding from the Legislature in prior years, and as of this writing we are in the midst of a Notice of Funding Availability making \$5 million available in gap financing for affordable housing preservation for use with the 4% LIHTC program. In our Agency Requested Budget, we

requested \$10 million in lottery backed bonds to be utilized for gap funding for multiple purposes, preservation being one of those. If approved, this gap funding would allow us to preserve an estimated 200 homes. We appreciate the examples provided in the audit from other states and will also be reaching out to other state housing agencies to learn of additional best practices.

Recommendation: Consider working with the Legislature to expand the Oregon Affordable Housing Tax Credit program.

Response: We would be happy to work with the legislature to discuss the potential for expansion of the OAHTC.

Strategic Planning

Recommendation: Engage in long-term, comprehensive strategic planning to create a vision for affordable housing and set the stage for the agency to provide leadership on housing issues. Develop a plan with input from all levels of the organization that incorporates the agency's mission, performance metrics, and goals specific to each section of the agency.

Response: As noted above in the letter, OHCS has been in the process of developing a Statewide Housing Plan as required by statute and we are excited that this plan will use data and research to guide the agency and the Housing Stability Council in their efforts to address Oregon's housing crisis. We are also going to be developing annual measurable goals for the agency and the calendar year 2017 goals are already being considered and shaped. In 2017 leadership will also be engaging the Agency, from staff to the members of the Housing Stability Council, in the development of a five year strategic plan that will guide the work of the Agency. The plan will include clear annual goals and performance metrics and provide a framework for reporting the Agency's outcomes on an annual basis.

Data Management

Recommendation: Review current IT capacity and incorporate strategies to address capacity needs and issues into the formal strategic plan.

Response: We agree with this recommendation and have actively worked to address this need. Actions taken include analyzing gaps in capacity, creating business cases to identify options to address the gaps, adding temporary resources when available, and requesting requisite resources through the budget process. We will continue to monitor this closely to ensure the resources available help inform and align with the strategic plan.

Recommendation: Define portfolio and identify properties within it.

Response: We agree with this recommendation and are taking steps to address this through the data systems modernization project. The updated data system will contain a formal

data dictionary, naming conventions, and system controls to ensure common understandings of data elements.

Recommendation: Identify and collect data elements to inform decision-making for underwriting and asset management.

Response: We agree with this recommendation and are ensuring completeness and accuracy of these elements prior to migration of the data into the new data system.

Recommendation: Consider developing systems to track operating expenses on an ongoing basis to provide a foundation for underwriting standards.

Response: We agree with this recommendation and are currently populating this information in the Asset Management module in our current system of record, HDS. This information should be useable in the next 4-6 months. This functionality will also be a required element in the Request for Proposal to procure an integrated data system.

Recommendation: Continue to collect property information to develop a single reliable source of all affordable properties in the state.

Response: We agree with this recommendation and have been engaged with a workgroup since the beginning of 2016 to ensure all data sources are accounted for and the data included is accurate and reliable. OHCS also requested staffing resources in its Agency Request Budget to provide the capacity needed to establish and maintain a robust affordable housing inventory for the State

Organizational Challenges

Recommendation: Consider filling the internal auditor position to help conduct risk assessments and to ensure strong internal controls are in place.

Response: We agree with the need for a risk assessment and strong internal controls. OHCS has been exempt from internal audit requirements since 2013 and that exemption ends in fiscal year 2017. We will ensure a risk assessment is completed as part of the internal audit work in 2017, and meanwhile are actively working to ensure strong internal controls are executed.

Recommendation: Improve communication and transparency with the Housing Stability Council.

Response: This is an important issue and we are taking immediate action with a council retreat tentatively scheduled for January 2017 to develop better communication and transparency with the council. The retreat will include discussion about the role of the new council going forward, and also a discussion of training or information needed to better equip Council members to perform their roles on the Council.

Recommendation: Involve staff and incorporate their feedback in decisions that impact their work.

Response: Our staff has tremendous experience, energy and ideas for how to move the agency forward. We will be developing a comprehensive employee engagement platform and including this work in our strategic plans.

Recommendation: Work with the Legislature and Housing Stability Council to clarify in statute the roles of the OHCS director and Housing Stability Council in leading the agency.

Response: We recognize the unclear direction that statute creates in terms of the work of the Housing Stability Council. We will be working with our legal counsel and the Housing Stability Council to see what may need to be done to correct this and better define the work and role of the Housing Stability Council.

Recommendation: Update and document processes for underwriting, including formal written policies and procedures, and guidance for loan officers.

Response: We agree this is critical. The data systems work will inform this and Multifamily staff will create written procedures as part of its continuous process improvement work.

Recommendation: Strengthen the conflict of interest policy and ensure it is followed.

Response: We are bringing in the Ethics Commission as part of our training for the Housing Stability Council and will also be sharing that training with appropriate staff.

Recommendation: Improve and document processes for contracting, including formal written policies and procedures.

Response: We agree with this recommendation and have already completed and adopted a number of formal policies and procedures to guide procurement and contracting work. We have identified remaining policies and procedures to develop and have created a work plan to ensure they are adopted by the middle of 2017.

Recommendation: Ensure contractors' performance is adequately monitored and deliverables are received.

Response: We agree with this recommendation and will incorporate performance monitoring requirements as part of the policies and procedure mentioned above. Additionally we intend of providing education and training in alignment with requirements under HB2375 to ensure procurement staff and contract administrators understand their roles and responsibilities related to performance monitoring of contractors.

We recommend the Housing Stability Council:

Recommendation: Work with the agency and Legislature to clarify its role.

Response: The Housing Stability Council members agree with this recommendation and will be working with myself, the executive team and staff to implement.

Recommendation: Communicate the Council's training and information needs to agency management.

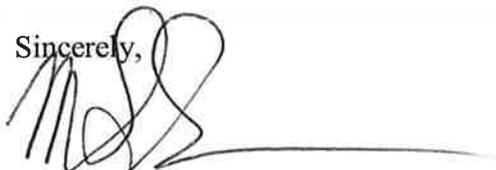
Response: Council members agree and this will be part of the regular communication between the agency and the council.

I hope that the responses and plan for implementation outlined above are received well by you and the audit team. Again, this audit provides valuable information for OHCS leadership and staff as we move forward into a very ambitious agenda. We know the housing crisis is not going away in the near future.

I would like to end our response with some examples of the good work the agency has done even during a very difficult transition effort and through changes in leadership. In 2015 OHCS funded 1,549 units of affordable housing, created 368 loans for first-time homebuyers through our Oregon Bond Loan program, and helped 2,252 homeowners avoid foreclosure through our Mortgage Payment Assistance program. Our Individual Development Account program is helping approximately 3,400 Oregonians save for future investments like education and homeownership. The agency has also provided homeless funds to over 15,000 families in need of assistance and helped over 81,000 low-income families in need of energy bill payment assistance.

As you can see, we have been hard at work and we are excited about our work ahead.

Sincerely,

A handwritten signature in black ink, appearing to read 'MS Salazar', with a long horizontal line extending to the right.

Margaret Solle Salazar

Office of the Secretary of State

Jeanne. P. Atkins
Secretary of State

Robert Taylor
Deputy Secretary of State



Audits Division

Mary Wenger
Interim Director

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Salem, OR 97310

(503) 986-2255

February 29, 2016

Margaret Van Vliet, Director
Oregon Housing and Community Services Department
725 Summer Street NE, Suite B
Salem, OR 97301-1266

Dear Ms. Van Vliet:

We have completed audit work of the following selected federal program at the Oregon Housing and Community Services Department (department) for the year ended June 30, 2015.

<u>CFDA Number</u>	<u>Program Name</u>	<u>Audit Amount</u>
93.568	Low-Income Home Energy Assistance (LIHEAP)	\$ 33,605,176

This audit work was not a comprehensive audit of your federal program. We performed this federal compliance audit as part of our annual Statewide Single Audit. The Single Audit is a very specific and discrete set of tests to determine compliance with federal funding requirements, and does not conclude on general efficiency, effectiveness, or state-specific compliance issues. The Office of Management and Budget (OMB) Circular A-133 identifies internal control and compliance requirements for federal programs. Auditors review and test internal controls for all federal programs selected for audit and perform specific audit procedures only for those compliance requirements that are direct and material to the federal program under audit. For the year ended June 30, 2015, we determined whether the department substantially complied with the following compliance requirements relevant to the federal program.

Compliance Requirement	General Summary of Audit Procedures Performed
Cash Management	Confirmed program costs were paid for before federal reimbursement was requested, or federal cash drawn was for an immediate need.
Period of Performance	Determined whether federal funds were used only during the authorized period of performance.
Reporting	Verified the department submitted financial and performance reports to the federal government in accordance with the grant agreement and that those financial reports were supported by the accounting records.

Compliance Requirement	General Summary of Audit Procedures Performed
Subrecipient Monitoring	Determined whether the pass-through entity monitored subrecipient activities to provide reasonable assurance that the subrecipient administers federal awards in compliance with federal requirements.

Noncompliance

Noncompliance is a failure to follow compliance requirements, or a violation of prohibitions included in compliance requirements, that are applicable to a federal program. As described in the “Audit Findings and Recommendations” section, we identified noncompliance with federal requirements which is required to be reported in accordance with OMB Circular A-133.

Internal Control Over Compliance

Department management is responsible for establishing and maintaining effective internal control over compliance with program requirements. In planning and performing our audit, we considered the department’s internal control over compliance with requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on the department’s compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the department’s internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described above and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. As discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses.

Audit Findings and Recommendations

Improve Reviews of Subrecipients

Federal Awarding Agency: U.S. Department of Health and Human Services
Program Title and CFDA Number: Low-Income Home Energy Assistance, CFDA 93.568
Federal Award Numbers and Year: 2015G992201; 2015, 2015G992205; 2015,
2015G992212; 2015, 2014G992201; 2014,
2014G995623; 2014
Compliance Requirement: Subrecipient Monitoring
Type of Finding: Material Weakness, Noncompliance

Federal regulations require the department, as a recipient of federal awards, to monitor the activities of subrecipients to ensure that federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements. For the LIHEAP program, this includes monitoring subrecipients to ensure:

- Program funds are used for certain allowable activities;
- Specified “earmarking” limits are not exceeded; and
- Subrecipient cost allocation plans are in compliance with applicable cost principles.

We found the department does not have adequate controls to ensure only costs for allowable activities are reimbursed with federal funds; limitations are not exceeded; and ensure subrecipients follow general cost principles, including gaining assurances that expenditures charged to federal programs are reasonable, equitably distributed, and adequately documented.

This has been an ongoing finding since fiscal year 2012 due to a lack of adequate resources dedicated by the department to develop and maintain adequate controls. The department has been in the process of updating its fiscal monitoring controls but has yet to fully implement changes to ensure compliance with program requirements.

We recommend department management complete and implement an adequate fiscal monitoring process to ensure federal reimbursements are for allowable program activities, subrecipient cost allocation plans are sufficiently reviewed to determine whether the plans are in compliance with applicable cost principles, and required limitations are not exceeded.

Strengthen Controls Over Cash Management

Federal Awarding Agency: U.S. Department of Health and Human Services
Program Title and CFDA Number: Low-Income Home Energy Assistance, CFDA 93.568
Federal Award Numbers and Year: 2015G992201; 2015, 2015G992205; 2015,
2015G992212; 2015, 2014G992201; 2014,
2014G995623; 2014
Compliance Requirement: Cash Management
Type of Finding: Material Weakness, Noncompliance

Federal regulations require program costs be paid with entity funds before reimbursement is requested from the federal government. The exception to the cost reimbursement basis is the

advancement of federal monies to meet immediate cash needs. When awards provide for advance payments, recipients must follow procedures to minimize the time elapsing between the transfer of funds from the U.S. Treasury and disbursement by the recipient with similar procedures established for subrecipients. These regulations include expectations for the department to monitor cash drawdowns by subrecipients to ensure subrecipients conform substantially to the same standards of timing and amounts that apply to the department.

We found the department does not have adequate controls to ensure funds are provided as reimbursement of costs already paid by the subrecipient or that a minimal lapse of time occurred between the advancement to and disbursement of funds by subrecipients. This has been an ongoing finding since fiscal year 2010 due to a lack of adequate resources dedicated by the department to develop and maintain an adequate control process. The department has been in the process of updating its reviews of subrecipient requests for funds but has yet to fully implement changes to ensure compliance with cash management requirements.

We recommend department management complete and implement adequate controls to ensure subrecipient requests for funds are in compliance with federal cash management requirements.

Prior Year Findings

In the prior fiscal years, we reported noncompliance and internal control findings in the Statewide Single Audit Report related to LIHEAP. For the fiscal-year ended June 30, 2014; see Secretary of State audit report number 2015-05, and for the fiscal year ended June 30, 2013; see Secretary of State audit report number 2014-09.

During fiscal year 2015, the department continued to develop plans for addressing these findings. The last two years of prior findings listed below will be reported in the Statewide Single Audit Report for the fiscal year ended June 30, 2015 with a status of partial corrective action taken.

Finding Title	Prior Year Finding No.
Review of Subrecipient Costs for Allowability Should be Improved	2013-046
Strengthen Controls Over Cash Management	2013-047
Improve Controls Over Subrecipient Cost Allocation Plans	2013-048
Improve Reviews of Subrecipients	2014-036
Improve Reviews of Subrecipient Allocated Costs	2014-037
Strengthen Controls Over Cash Management	2014-038

The audit findings and recommendations above, along with your responses, will be included in our Statewide Single Audit Report for the fiscal year ended June 30, 2015. Including your responses satisfies the federal requirement that management prepare a Corrective Action Plan covering all reported audit findings. Satisfying the federal requirement in this manner,

Margaret Van Vliet, Director
Oregon Housing and Community Services Department
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however, can only be accomplished if the response to each material weakness includes the information specified by the federal requirement, and only if the responses are received in time to be included in the audit report. The following information is required for the each response:

- 1) Your agreement or disagreement with the finding. If you do not agree with an audit finding or believe corrective action is not required, include in your response an explanation and specific reasons for your position.
- 2) The corrective action planned.
- 3) The anticipated completion date.
- 4) The name(s) of the contact person(s) responsible for corrective action.

Please provide a response to us by March 7, 2016 and provide Rob Hamilton, Statewide Accounting and Reporting Services (SARS) Manager, a copy of your Corrective Action Plan.

The purpose of this communication is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this communication is not suitable for any other purpose.

We appreciate your staff's assistance and cooperation during this audit. Should you have any questions, please contact Wendy Hewitt, Principal Auditor or Julianne Kennedy, Audit Manager at (503) 986-2255.

Sincerely,

Office of the Secretary of State, Audits Division

cc: Caleb Yant, CFO
Claire Seguin, Assistant Director of Housing Stabilization
Sandra Flickinger, Financial Services Section Manager
Tim Zimmer, Energy and Weatherization Section Manager
George Naughton, Interim Director, Department of Administrative Services