September 16, 2021

2021-615.1

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

This report provides an update on our assessment of the State’s management of funding provided to the states by the federal government to address the impacts of the COVID-19 pandemic (federal COVID-19 funding) as a high-risk statewide issue. In August 2020, we designated the State’s management of federal COVID-19 funds as high risk after concluding that the likelihood of mismanagement of these funds is great enough to create substantial risk of serious detriment to the State and its residents. The Department of Housing and Community Development (HCD) manages $1.8 billion to administer California’s program to provide rental assistance benefits to eligible households with residents at risk of eviction. This report focuses exclusively on HCD’s progress in committing and awarding rent relief program benefits to eligible California households by the first crucial federal deadline, which is September 30, 2021.

Because of the looming deadline and effect it may have on the State if critical requirements are not met, it is important to issue this first report of our audit to notify you of the urgent risk of losing federal funds that the State faces. Given the narrow time frame set by the federal government, we wanted to impress upon you the need for continued attention in order to minimize the risk and the amount of funds the State could lose beginning September 30, 2021. We plan to issue a separate audit report in 2022 that will evaluate HCD’s management of the federal COVID-19 funding for the rental assistance program. Although HCD is making significant progress toward meeting the first federal deadline, it must commit additional benefits to eligible households in order to reduce the State’s risk of losing millions of dollars in federal funds for this program at the end of September 2021.

Background

Since the spread of COVID-19 reached pandemic proportions in March 2020, Congress has enacted various laws to provide funds to Americans and to state and local governments for basic needs related to the pandemic’s economic impact. As unemployment surged in 2020, many Americans struggled to make monthly rent and utility payments, both of which Congress considers to be key components of stable housing.

To support those faced with possible evictions from their homes, Congress established a nationwide Emergency Rental Assistance program (ERAP) through the Consolidated Appropriations Act, 2021, in December 2020. This federal law required the U.S. Department of
the Treasury (Treasury) to provide states and local jurisdictions—cities and counties—with populations greater than 200,000 (federal grantees) with funding to provide their residents with rental assistance. In March 2021, Congress passed the American Rescue Plan Act of 2021, which established a second round of ERAP funding for federal grantees. We refer to the initial round of ERAP funds from the Consolidated Appropriations Act, 2021, as Round 1 and the second round of ERAP funds from the American Rescue Plan Act of 2021 as Round 2. California used its $1.5 billion of Round 1 ERAP funds to develop a new rental assistance program in January 2021, and the Legislature assigned HCD to administer the program.

Federal law established different timelines and requirements for Round 1 and Round 2 funding. To mitigate the impact of potential widespread evictions during the pandemic, Round 1 federal grantees must provide specific assistance to eligible households for existing debt and future rent or utilities payments (rental assistance). However, for Round 2, federal grantees can also use the funding more broadly for other affordable rental housing and eviction prevention activities beginning in late 2022. The text box shows that the eligibility requirements are the same for both rounds of funding, but Round 1 has a much shorter timeline for spending than Round 2. To ensure that the funds quickly get to those who need them, the Round 1 federal program requirements specify that Treasury must recapture all funds that federal grantees have not obligated beginning on September 30, 2021. Treasury has defined obligated funds as the total amount of funds a federal grantee has approved for payment to or for participating households and for a federal grantee’s approved administrative expenses. Treasury must then reallocate these recaptured funds to other eligible federal grantees—those that have obligated at least 65 percent of their original allocations and that demonstrate a need for them. Federal grantees have until September 30, 2022, to spend all of their Round 1 funds and until September 30, 2025, to spend all of their Round 2 funds. This report focuses on HCD’s efforts to meet the September 30, 2021, deadline for obligating as much of the State’s Round 1 funds as possible.

As Figure 1 shows, California received a total of $2.6 billion in Round 1 ERAP funds: Treasury appropriated $1.5 billion to the State and $1.1 billion directly to 49 cities and counties with a population of 200,000 or more. In January 2021, using the federal allocation to the State, the Legislature created a rent relief program, which directed HCD to allocate its $1.5 billion throughout the State based on population, including to those 49 local jurisdictions that received direct federal allocations and the 30 counties with populations less than 200,000 (small counties) that did not receive funds directly from Treasury. State law requires HCD to administer the rental assistance program for those 30 small counties. Of the 49 local jurisdictions that received direct federal allocations, 27 opted to have HCD administer their

---

**Households Eligible for ERAP Benefits Under Federal Law**

Applicants must meet all of the following criteria:

- Income of less than 80 percent of the area median income (AMI).
- Experienced financial hardship because of the pandemic, such as unemployment.
- Demonstrated risk of experiencing homelessness or housing instability.

Source: Federal law.

---

1 Although the eligibility requirements are the same for both rounds of funding, Round 1 applicants must also attest in writing that one or more individuals in the household experienced a reduction in income, incurred significant costs, or experienced other financial hardship because of the COVID-19 pandemic.

2 The area median income (AMI) is the midpoint of a region’s income distribution, meaning that half of the households in the region earn more than the median and half earn less than the median.
portions of the state allocation through the State’s rental assistance program. Eleven of these 27 jurisdictions also transferred their direct federal allocations, totaling $292 million, to HCD to administer on their behalf. As we describe below, the remaining 22 local jurisdictions that received direct federal allocations requested block grants—grants from HCD of their portion of the State’s allocation—to administer local rent relief programs on their own using both their federal allocations and their block grants from the State. HCD does not have oversight of any of the $821 million in other direct federal allocations that Treasury paid directly to the remaining 38 federal grantees.

Figure 1
HCD Is Responsible for $1.8 Billion in Round 1 ERAP Funds

State law also allows HCD to provide funding through block grants to certain local jurisdictions that operate their own local rental assistance programs instead of participating in HCD’s statewide program (state grantees). These block grants allow state grantees to receive their portion of the state allocation to administer their own local rental assistance programs.
independently from HCD. Twenty-two jurisdictions with populations greater than 200,000
opted to receive block grants totaling $553 million to administer their local rental assistance
programs in conjunction with their direct federal allocations from Treasury. For example,
San Diego County received a direct federal allocation from Treasury of nearly $49 million and a
block grant from HCD of $59 million to administer a local rental assistance program of almost
$108 million for its residents. However, as the original recipient of the federal funding used for
these block grants, HCD remains responsible for ensuring that the obligation of the block grant
funds complies with Treasury’s deadline. Therefore, in total, HCD is responsible for overseeing
$1.8 billion in federal Round 1 ERAP funding.

As authorized by state law, HCD contracted with a
vendor to implement and administer the State’s rental
assistance program. State law requires that the vendor
have sufficient capacity and experience to manage the
State’s rental assistance program services and distribute
funding to eligible applicants. HCD entered into a
contract for these services on March 4, 2021. HCD’s
vendor established its online application system in time
to accept its first application by March 15, 2021, as the
law required. The vendor is responsible for accepting
and reviewing all rental assistance applications,
including determining eligibility, and disbursing benefit
funds to approved applicants for the 57 jurisdictions
that are participating in HCD’s state rental assistance program. As part of its administration,
state law requires HCD to prioritize payments for the applicants who fall within the populations
described in the text box.

As explained above, the 22 state grantees—local jurisdictions that requested block grants from
HCD—administer their rental assistance programs independently from HCD. As part of this
local administration, state grantees are responsible for reviewing and processing applications
from residents in their jurisdictions and for paying rental assistance benefits to approved
applicants. State law requires state grantees to report to HCD weekly on the amount of funding
they have obligated and the amount of benefits they have paid. In order to ensure that the State
qualifies for the federal reallocation after September 30, 2021, state law authorized HCD to
reallocating unused local rental assistance funds from the state grantees that had not obligated at
least 65 percent of their block grants by June 1, 2021.

The Legislature subsequently revised state law and, as a result, local jurisdictions that received
block grants had additional time to obligate their rental assistance funds before HCD could
begin to reallocate unused funds in advance of the federal September 30, 2021, deadline.
Specifically, the revised law requires state grantees to obligate at least 65 percent of their
Round 1 block grant funds by August 1, 2021. State grantees that failed to meet this requirement
must repay to HCD any unused block grant funds not obligated or spent at that time. HCD may
then reallocate those funds to other eligible local jurisdictions based on certain factors, such as
unmet need. This reallocation process allows California to obligate as much rental assistance
funding as possible to eligible households before the federal deadline of September 30, 2021.
The revised state law also extended the State’s eviction moratorium through the end of
September 2021. Figure 2 shows a timeline of California’s establishment of ERAP and progress
in obligating federal funds.

### Households Prioritized for Rental Assistance Benefits in California

1. Extremely and very low-income, earning less than
   50 percent of their local AMI.
2. Communities disproportionately impacted by COVID-19,
   as determined by HCD.
3. Lower income, earning less than 80 percent of their AMI.

Source: State law and HCD’s definitions of income limits.
Figure 2
California Had Nine Months to Obligate as Much of Its $1.8 Billion in ERAP Funding as Possible

Federal Actions
State Actions
HCD Actions
Outdated Requirements

Percent of HCD’s total obligated funds

2020
DECEMBER 27, 2020
Consolidated Appropriations Act, 2021, establishes ERAP and allocates Round 1 funding.

JANUARY 19, 2021
Treasury issues first set of formalized guidance for ERAP Round 1.

JANUARY 29
State law established stricter requirements for California’s rent relief program than federal law, including allowing only 80 percent in assistance for rental debt and requiring landlords to forgive the remaining 20 percent; allowed certain local jurisdictions to opt into HCD’s program or request block grant funding for Round 1 implementation.

FEBRUARY 22
Treasury provides revised guidance for ERAP.

MARCH 4
HCD hires a vendor to administer its statewide program.

MARCH 11
American Rescue Plan Act of 2021 adds $2.6 billion in Round 2 ERAP funding for California.

MARCH 15
Program launches when HCD begins accepting rental assistance applications.

APRIL 12
HCD issues first rental assistance payments.

MARCH 11
American Rescue Plan Act of 2021 adds $2.6 billion in Round 2 ERAP funding for California.

MAY 7
Treasury revises and updates guidance for ERAP.

JUNE 1
State grantees must obligate at least 65 percent of their block grants and repay any unused funds not obligated or spent to HCD for reallocation.

JUNE 4
HCD submits the first monthly report to the Joint Legislative Budget Committee, providing data about its progress and the program’s performance since its launch in March.

MAY 31
14%

JUNE 30
27%

JULY 31
43%

SEPTEMBER 1
76%

SEPTEMBER 8
81%

2021

Source: Federal and state laws, Treasury guidance, and HCD program documentation, including unaudited data from HCD’s data dashboard for ERAP funding.
Under federal law, Treasury must recapture unobligated funds for the ERAP program beginning on September 30, 2021. Additionally, federal law provides that HCD will only be eligible to receive another allocation of these recaptured funds from Treasury if it has obligated at least 65 percent of the $1.8 billion total allocation for which it is responsible, or $1.2 billion. Treasury must base its reallocation decisions on the demonstrated need within a federal grantee’s jurisdiction.

**Although HCD Has Defined Its Obligated Funds In Alignment With Treasury’s Guidance, It Did Not Use That Definition in Its Recent Report to Treasury**

Although Treasury did not issue guidance that defines obligated funds until late June 2021, HCD developed a definition of obligated funds to report to the Legislature. State law requires HCD to report to the Legislature monthly on its obligation of funds for rental assistance as well as other program data, which required HCD to establish a definition of obligated funds in the absence of Treasury guidance. In its first report to the Legislature on June 4, 2021, HCD defined funds as obligated when the funds had been identified for and committed to an eligible household pending final application approval. HCD’s glossary for its data dashboard further explains that these funds are committed when its vendor has reviewed a resident’s application and preliminarily approved the applicant as eligible for rental assistance benefits. According to the vendor’s procedures, before preliminarily approving an application, the vendor reviews documentation to verify the applicant’s eligibility, including validating household income and rent calculations. For purposes of reporting obligated funds to its data dashboard and to the Legislature, HCD uses these amounts to represent HCD’s commitment to pay these funds. After an application is preliminarily approved, HCD’s vendor performs its quality control reviews, which include, for example, checking for duplication of benefits and potential fraud before paying benefits to approved households. In its initial reporting guidance on June 30, 2021, Treasury provides that federal grantees may use a definition contained in existing policies and procedures, which indicates the amount obligated should reflect the amount of payments to or for participating households that the federal grantee has agreed to pay. Therefore, HCD has taken a reasonable approach in defining its amount of obligated funds as those preliminarily approved because this approach aligns with Treasury’s reporting guidance.

However, HCD has been inconsistent in how it has reported its obligated funds to Treasury and the Legislature. HCD reported a total of $446 million in obligated funds to the Legislature through the end of June 2021, using its definition of obligated funds—those funds preliminarily approved for applicants. It also reported obligated funds using this definition to the Legislature through July 2021. However, HCD reported to Treasury that it had obligated $1.6 billion—90 percent of its funds—in its rental assistance program through the end of June 2021. HCD explained that this new total obligated amount includes its forecast of payments to eligible households to further demonstrate the ongoing need in California, and that it calculated this amount by using the average monthly assistance approved for each household and forecasted it for the allowable program period (15 months). In August 2021, HCD’s data dashboard began showing this new calculation of obligated funds as more than $1.9 billion in total obligated assistance.

By reporting its obligated funds in this way, HCD’s approach does not align with Treasury’s reporting guidance and risks overstating its obligated amounts to Treasury. Therefore, despite HCD’s reporting to Treasury in August 2021 that it had obligated 90 percent of its Round 1 funds, Treasury may reject HCD’s method of interpreting its obligated totals when it
assesses them after September 30, 2021. HCD stated that because Treasury has not indicated the exact formula it will use to determine funds obligated under federal statute, HCD has developed several models of potential interpretations. HCD explained that the model it reported to Treasury, which forecasts obligation totals, is similar to obligation calculations it has used for other federally funded housing-related programs for which it must obligate the full amount of funding an eligible household can expect to receive over the life of the program. It further explained that by failing to obligate funds that eligible households may receive in the future, programs risk exhausting available funds before recipients gain their full allowed benefit. Although federal law requires Treasury to base any reallocation amounts on demonstrated need within a grantee’s jurisdiction beginning on September 30, 2021, Treasury’s reporting guidance does not direct federal grantees to report on any data related to forecasted or future need. Therefore, the risk exists that Treasury will not accept HCD’s reporting of obligation amounts that are based on forecasted obligation totals. Moreover, another of HCD’s models uses its definition of obligated funds that aligns with current Treasury guidance. As we note in the next section, our analysis based on this model shows that HCD had obligated 81 percent of its total as of September 8, 2021.

Despite Its Progress in Obligating Rental Assistance Benefits, HCD Remains at Risk of Losing Federal Funds

HCD remains at risk of losing federal funds, and it must employ every effort possible to increase its amount of funds obligated before the federal deadline of September 30, 2021. Since its first report to the Legislature on June 4, 2021, HCD’s data indicate substantial progress in the amount it has obligated and the amount paid for rental assistance. Through September 8, 2021, HCD’s data show that it has increased its obligated amount to more than $1.4 billion, or 81 percent of its $1.8 billion in allocated funds from Treasury. Therefore, HCD is eligible for reallocated funds from Treasury after September 30, 2021. However, it continues to be important that HCD obligate as much of the $1.8 billion as possible so that the State is in the best position to potentially receive additional federal funds for rental assistance. Specifically, if HCD does not obligate any funds beyond this 81 percent by September 30, 2021, it may lose up to $337 million of its remaining unobligated funds, but it would remain eligible for a portion of the Round 1 reallocated funds from Treasury.

Based on rental assistance amounts requested, California residents still have a demonstrated need for rental assistance. As of September 8, 2021, HCD reported that it had received applications for rental assistance totaling more than $993 million and for utilities assistance totaling $108 million that it has not yet processed. Although these requested benefits do not apply toward HCD’s obligation total for the September 30, 2021, federal deadline, it indicates that there is enough demand for HCD to demonstrate additional need for reallocated funds from Treasury. Federal law requires Treasury to base its reallocation decisions on the demonstrated need of federal grantees. In California, the demand for rental assistance varies by local jurisdiction, with some local jurisdictions receiving applications that far exceed their original allocation of funds from HCD. For example, the City and County of San Francisco (San Francisco) received an allocation from HCD of $29 million, but HCD’s data dashboard as of September 8, 2021, reports receiving applications from San Francisco households totaling more than $76 million, leaving an unmet demand of $47 million, if all applications are valid. Other large jurisdictions under HCD’s administration have experienced similar levels of demand. Moreover, as we show in Figure 1, because 22 jurisdictions within California operate
their local rental assistance programs independently from HCD using block grants and their direct federal allocations, there is likely additional demand for rental assistance within those jurisdictions that HCD’s data do not include.

**Changes to the State’s Rent Relief Program Have Slowed HCD’s Ability to Reallocate Funds Throughout the State**

In June 2021, state law changed requirements for the rent relief program, and incorporating these changes has delayed HCD’s original plan to reallocate funds in August 2021 ahead of the September 30, 2021, federal deadline. Amended state law allowed state grantees to request a change to their option for administering their rental assistance programs for Round 1 or Round 2 funds, subject to HCD’s approval. After the revisions to state law that became effective in late June 2021, HCD allowed the 49 federal grantees within the State to change their administrative option in July 2021 for implementing Round 1. Specifically, HCD invited jurisdictions to join HCD’s statewide program or to request block grants to help minimize confusion among residents, streamline application processing, and enable timely payments using all available funds. HCD explained that in order to properly administer ERAP and ensure that there is no duplication of benefits, it must consolidate and account for the Round 1 rental assistance funds for each jurisdiction that changes its administrative option before HCD can reallocate funds to other areas within the State.

It has taken HCD time to process the administrative changes to the rental assistance program, which has delayed its ability to reallocate funds. Amended state law also requires local jurisdictions that received block grant funds from HCD to have obligated at least 65 percent of their block grant funds by August 1, 2021. For grantees that did not meet this requirement, state law requires them to repay funds to HCD that they have not obligated or spent and allows HCD to reallocate these funds to other jurisdictions that demonstrate a need for additional funds. However, state law also authorizes HCD to waive the requirement for state grantees to repay these funds, if the grantees demonstrate that they will obligate and spend any unused block grants within the federal law time frames. For those funds that HCD reallocates, state law requires HCD to prioritize this reallocation of funds to other local jurisdictions based on factors such as unmet need and rate of application submissions.

As of September 8, 2021, HCD had not reallocated any unused funds. Although 22 local jurisdictions requested block grants from HCD totaling $553 million to operate their own rental assistance programs, HCD had only transferred block grant funds totaling $426 million to 14 state grantees that have completed their agreements with HCD. According to the department, the remaining eight grantees have either chosen to join HCD’s statewide rental assistance program or are in the process of finalizing local approval for their agreements with HCD. Although HCD still has access to the block grant funds for these eight state grantees without signed agreements, HCD explained that it must finalize the changes to local jurisdictions’ administrative options before reallocating funds from Round 1.

Although HCD originally planned to reallocate funds in early August 2021 from the state grantees that had not obligated at least 65 percent of their block grants, HCD explained that program changes delayed its ability to do so. HCD staff explained that the department does not want to reallocate funding away from jurisdictions where there continues to be need and the capacity to move the resources in a timely manner. Further, HCD explained that permanently
reallocating funds now could force it to move funds again once the jurisdictions have finalized their administrative options for Round 2. According to HCD, this would overcomplicate the process and make it more difficult for the department to track the funds. Regardless, the longer it takes HCD to finalize these administrative options in order to reallocate to other areas of the State with a demonstrated need, the less time HCD and local jurisdictions have available to maximize their obligation of funds before the impending September 30, 2021 deadline. Therefore, the State remains at risk of losing critical ERAP funds that are not obligated by the deadline.

Conclusion

Although HCD recently reported to Treasury that it has obligated 90 percent of its total ERAP funds based on forecasted totals, there is risk that Treasury may reject HCD’s interpretation of the obligated totals it reported. Using totals aligned with Treasury guidance, HCD surpassed the 65 percent obligation threshold, which makes it eligible to receive a reallocation from Treasury. However, it still risks losing any remaining unobligated funds because federal law requires Treasury to recapture unobligated funds beginning on September 30, 2021. Further, because Treasury has not guaranteed a reallocation to each eligible jurisdiction, HCD may not receive a reallocation from Treasury or, if it does, the reallocation may not adequately cover the current unmet need for rental assistance in California. Therefore, it is important that HCD obligates as much of the $1.8 billion as possible before September 30, 2021, so that the State minimizes its loss of critical federal funding.

Treasury has allocated an additional $2.6 billion to California and the 49 other federal grantees in California through Round 2 ERAP funding, which, when combined with Round 1 funding, totals $5.2 billion in funding for California’s rental assistance program. We plan to issue a separate audit report in 2022 that will evaluate HCD’s management of the federal COVID-19 funding for ERAP.

Agency Perspective

Because it interprets federal law differently, HCD disagrees with our conclusion that there is risk that Treasury will recapture any of its Round 1 ERAP funds beginning September 30, 2021.

We conducted this audit under the authority vested in the California State Auditor by Government Code section 8543 et seq. and according to generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives specified in the Scope and Methodology section of the report. We believe the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Respectfully submitted,

Elaine M. Howle

ELAINE M. HOWLE, CPA
California State Auditor
Scope and Methodology

State law authorizes the California State Auditor (State Auditor) to establish a program to audit and issue reports with recommendations to improve any state agency or statewide issue that we identify as being at high risk for the potential of waste, fraud, abuse, and mismanagement or that has major challenges associated with its economy, efficiency, or effectiveness. In August 2020, we issued a report that designated the State’s management of federal COVID-19 funds as a high-risk statewide issue in California. Because HCD administers the State’s rental assistance program, and specifically the Round 1 Consolidated Appropriations Act, 2021, federal funding related to rent relief due to loss of income from the COVID-19 pandemic, we performed an audit of HCD’s progress in obligating these rental assistance funds to eligible California households by the Consolidated Appropriations Act’s first crucial deadline of September 30, 2021. For the purposes of this audit, our primary objective was to assess the program’s progress in obligating and spending federal COVID-19 funds for ERAP to determine whether it will likely meet state and federal spending deadlines, and to evaluate HCD’s plans to reallocate funds as necessary from local jurisdictions unlikely to meet those deadlines. In conducting this audit, we interviewed staff at HCD, reviewed guidance from Treasury as well as state and federal requirements, and collected and reviewed program documentation from HCD pertaining to its efforts to obligate rental assistance funds.
September 3, 2021

Elaine M. Howle, CPA
California State Auditor
1621 Capitol Mall, Suite 1200
Sacramento, CA 95814

Re: Emergency Rental Assistance Program Audit

Dear Ms. Howle,

The Department of Housing and Community Development (HCD) acknowledges receipt of the California State Auditor's (CSA) review of HCD’s implementation of the Emergency Rental Assistance Program (ERAP), as set forth in CSA’s draft report submitted to HCD entitled “State High Risk Program 2021-615.1” (the “Report”). HCD provides this response on behalf of itself and the Business, Consumer Services and Housing Agency.

The subject of the Report, the ERAP program, has helped nearly 50,000 households by providing both rental and utility assistance for tenant households that are at or below extremely low-income levels. This has resulted in nearly $1.4 billion in requested assistance, and nearly $500 million paid to date. ERAP has helped to avoid a cascade of residential evictions, especially as State and Federal eviction protections expire or are eliminated by the courts.

Although not mandated, HCD appreciates this opportunity to comment on the Report. First and foremost, we appreciate CSA acknowledging, in the Report, that “HCD is making significant progress toward meeting the first federal deadline.” We also appreciate the Report's statement that “HCD has taken a reasonable approach in defining its amount of obligated funds.” Lastly, we are grateful the Report acknowledges that external factors, such as changes to governing law, as well as uncertainty in Federal guidance, have presented challenges for HCD to overcome - and that thus far HCD’s approach to addressing these has been appropriate. There are, however, other matters referenced in the Report that we think merit more treatment. Thus, we provide comment on them here.

HCD is unlikely to lose the subject funding so long as HCD meets the 65% threshold. Per the federal statute:

“Beginning on September 30, 2021, the Secretary shall recapture excess funds, as determined by the Secretary, not obligated by a grantee for the purposes described under subsection (c) and the Secretary shall reallocate and repay such amounts to eligible grantees who, at the time of such reallocation, have obligated at least 65 percent of the amount originally allocated and paid to such grantee...”

1

In the Report, CSA suggests, based on a plain language strict constructionist reading of the statute, that beginning on September 30, 2021, the US Secretary of the Treasury (“Treasury”) must recapture all excess

1 Title V Banking, Subtitle A Emergency Rental Assistance, Section 501 Emergency Rental Assistance
funds that are not yet “obligated” pursuant to Section 501(d) of the Consolidated Appropriations Act, 2021. By contrast, HCD’s interpretation, which is informed by direct communications with Treasury officials, and upon advice from legal counsel, is that a recipient’s funds are recaptured only if the recipient falls below the 65% obligation threshold. If, on the other hand, the recipient has obligated at least 65% of its funds by September 30, 2021, then none of its funds will be recaptured by the Treasury. In fact, this seems to represent the more reasonable interpretation. Were it otherwise, the Secretary would have engaged in a futile act (i.e., recapturing funds on one day just to give them back, with more, on the next). Thus, while HCD acknowledges that the subject statute does not expressly state that the Secretary will not recapture funds if a recipient has obligated at least 65% of the funds, the statute implies that term by providing that the Secretary may only provide recaptured funds to recipients who have surpassed the 65% mark.

**HCD’s reporting of obligated funds to Treasury is appropriate given the ongoing discussions with Treasury and its changing Federal guidance.** Although the report comments that HCD has changed its reporting methodology to Treasury, the Report fails to give the context that HCD’s revisions are to show both conservative and projected needs to Treasury, all of which may meet the yet unknown final Federal guidance, when it becomes available. By providing alternate methods, HCD shows the need within the State tied to projections based on actual approved households, which Treasury stated it was interested in. The Report should link its discussion of these alternative methodologies with its discussion of a lack of a clear federal definition of “obligation.”

**The Auditor should consider postponing release of the Report until either October 1, 2021, or until Treasury provides further guidance.** As of the date of this response, HCD requested that the Report not be released until additional federal guidance was provided, or at least not until the actual assistance numbers were ascertained on September 30, 2021 (as required by the federal statute). Although that request was not granted, we renew the request here because intervening events will critically inform whether HCD’s calculations and performance to date presents any real risk. Instead, by releasing the report weeks in advance of the above, CSA and HCD must both admit uncertainty in evaluating the true level of remaining risk. Additionally, at the time of this response, HCD is: on track to exceed the 65% obligation measure on September 30, 2021 by already successfully obligating nearly 65% of funds as of September 10, 2021; and thus HCD is on track to receive additional funding from Treasury that will be recaptured from other grantees that are below the 65% mark. Clarity on both the foregoing would greatly be increased by waiting just a few weeks longer.

Thank you for this opportunity to respond. Should you have any questions, please contact HCD’s Chief Internal Auditor, Michael Mock, Michael.Mock@hcd.ca.gov.

Sincerely,

Gustavo F. Velasquez
Director

Cc: Lourdes M. Castro Ramírez, Secretary, California Business, Consumer Services and Housing Agency
CALIFORNIA STATE AUDITOR’S COMMENTS ON THE RESPONSE FROM THE DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT

To provide clarity and perspective, we are commenting on HCD’s response to our audit. The numbers below correspond to the numbers we have placed in the margins of HCD’s response.

1. We stand by our conclusion that HCD is at risk of losing any unobligated federal funds. As HCD’s response notes, the federal Consolidated Appropriations Act 2021, provides that, beginning on September 30, 2021, Treasury shall recapture excess funds not obligated for the Emergency Rental Assistance program. Our interpretation of the statute, based upon the plain language, is reasonable and conservative, particularly given the absence of written guidance from Treasury as to what actions it will take beginning September 30, 2021. HCD’s interpretation disregards the risk that we have identified that Treasury may, in fact, recapture HCD’s unobligated funds beginning September 30, 2021.

2. We recognize that HCD has had ongoing verbal communications with Treasury. However, HCD was unable to provide any written correspondence from Treasury regarding these discussions. In the absence of written and documented directives from Treasury, we must rely upon the public guidance Treasury has issued and the legal requirements outlined in federal and state law to form our conclusions.

3. We disagree that Treasury has not provided a clear definition of “obligation,” which we note in our report. Specifically, we acknowledge that HCD developed a reasonable definition for obligation before Treasury issued its guidance that defined obligation, and that HCD’s definition aligns with Treasury’s guidance issued on June 30, 2021. Our concern, as we describe on page 6, is that HCD’s decision to use an alternative methodology for reporting obligated funds does not align with Treasury’s reporting guidance, which risks Treasury rejecting HCD’s method of interpreting its obligated totals.

4. As we note in our first point above, HCD’s request here disregards the risk outlined in federal law that it may lose millions of dollars in federal rental assistance funds beginning September 30, 2021. Because Treasury has not issued any guidance describing what actions it plans to take beginning September 30, 2021, to recapture excess funds, there is uncertainty as to whether HCD will retain its total Round 1 allocation, as it asserts. Moreover, as we note on page 9, Treasury has not guaranteed a reallocation to each eligible jurisdiction. Therefore, we believe it is critical to issue this report to notify the Legislature and the public of the urgent risk related to the State’s Round 1 rent relief funding. We continue to encourage HCD to obligate as much of the funding as possible by September 30, 2021, to avoid losing critical funds for California’s residents.

5. Subsequent to sharing our draft report and receiving HCD’s response, we updated the report to reflect the amount HCD has obligated as of September 8, 2021. As we note on page 7, HCD obligated 81 percent of its total funds as of September 8, 2021.