Section 3. Financial Information

Acting Deputy Chief Financial Officer's Message

November 15, 2005

I am pleased to report on HUD's continuing financial management improvements during FY 2005. The Department was able to close the annual books on its significant program activity and produce audited consolidated financial statements within 45 days after the end of the fiscal year, with an unqualified audit opinion. This accomplishment is a result of systemic improvements and other corrective actions to strengthen internal controls and instill increased discipline in controls over financial reporting throughout the year, as evidenced by the following:

- Continuing efforts to improve internal controls over HUD's rental housing assistance payments eliminated a longstanding material weakness and reduced the $3.2 billion baseline estimate of improper payments established in FY 2000 to $1.4 billion, well exceeding the FY 2005 goal for a 50 percent reduction;
- A full year's operation of the new accounts payable, accounts receivable, procurement, and projects modules of the FHA Subsidiary Ledger Project strengthened support for FHA's cash management, funds control, and credit subsidy accounting functions and enabled the Department to eliminate another longstanding material weakness issue, and for the first time, to report substantial compliance with the Federal Financial Management Improvement Act of 1996 and Section 4 of the Federal Managers' Financial Integrity Act of 1982;
- A reconciliation and reconstruction of records for over 3,300 projects in the Section 236 Interest Reduction Program enabled HUD to establish a revised estimate of the remaining program run-out costs of nearly $5 billion, with provisions for an improved integration and automation of the program business and accounting processes to maintain accurate program balances going forward;
- Changes to Section 8 Program funding processes and methodologies for recapturing excess program funds addressed prior Inspector General audit concerns regarding large obligation balances on expired contracts and enabled HUD to recapture over $1.5 billion to meet enacted rescission mandates and other program needs; and
- Accounting operations met or exceeded OMB's financial performance metrics goals for producing quarterly financial statements and decreases in: fund balance with Treasury differences, aged suspense accounts, accounts receivables delinquencies, late payments of invoices, travel card delinquencies on both individually and centrally billed accounts, and purchase card delinquencies.

HUD is committed to maintaining proper stewardship of the resources entrusted to it by the Congress and the American taxpayer. I want to thank the staff of the Office of the Chief Financial Officer, the FHA and Ginnie Mae Comptroller's Offices, the Office of Inspector General, and other HUD program and administrative components that are involved in the stewardship of HUD's funds, for their dedication and effort in providing HUD's management team with the budgetary, accounting, financial management systems, auditing, and performance management services necessary to effectively support HUD's mission and deliver results for the American people.

James M. Martin
Acting Deputy Chief Financial Officer

Introduction to the Financial Statements

The principal financial statements have been prepared to report the financial position and results of operations of HUD, pursuant to the requirements of the Chief Financial Officers Act of 1990 (31 U.S.C. 3515(b)), the Government Management Reform Act of 1994, and OMB Circular No. A-136, "Financial Reporting Requirements." While the financial statements have been prepared from HUD's books and records in accordance with formats prescribed by OMB, the statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records.

The principal financial statements and notes should be read with the realization that they are for a component of the U.S. Government, a sovereign entity. One implication is that the liabilities reported in the financial statements cannot be liquidated without legislation that provides resources to do so.

The financial statements presented herein are:

The **Consolidated Balance Sheets**, which present as of September 30, 2005 and 2004 those resources owned or managed by HUD which are available to provide future economic benefits (assets); amounts owed by HUD that will require payments from those resources or future resources (liabilities); and residual amounts retained by HUD comprising the difference (net position).

The **Consolidated Statements of Net Cost**, which present the net cost of HUD operations for the years ended September 30, 2005 and 2004. HUD's net cost of operations includes the gross costs incurred by HUD less any exchange revenue earned from HUD activities.

The **Consolidated Statements of Changes in Net Position**, which present the change in HUD's net position resulting from the net cost of HUD operations, budgetary financing sources other than exchange revenues, and other financing sources for the years ended September 30, 2005 and 2004.

The **Combined Statements of Budgetary Resources**, which present the budgetary resources available to HUD during FY 2005 and 2004, the status of these resources at September 30, 2005 and 2004, and the outlay of budgetary resources for the years ended September 30, 2005 and 2004.

The **Consolidated Statements of Financing**, which reconcile the net cost of operations with the obligation of budgetary resources for the years ended September 30, 2005 and 2004.

The **Notes to the Financial Statements** provide important disclosures and details related to information reported on the statements.

Consolidated Balance Sheet
As of September 30, 2005 and 2004
(Dollars in millions)

	2005	2004 Restated
ASSETS		
Intragovernmental		
Fund Balance with Treasury (Note 3)	$67,500	$69,647
Investments (Note 5)	30,715	31,029
Other Assets (Note 8)	28	21
Total Intragovernmental Assets (Note 6)	$98,243	$100,697
Investments (Net) (Note 5)	201	122
Accounts Receivable (Net) (Note 7)	646	491
Credit Program Receivables and Related Foreclosed Property (Net) (Note 9)	10,818	11,238
General Property Plant and Equipment (Net) (Note 10)	141	96
Other Assets (Note 8)	520	550
TOTAL ASSETS (Note 6)	$110,569	$113,194
LIABILITIES		
Intragovernmental Liabilities		
Debt (Note 12)	$8,922	$10,102
Other Intragovernmental Liabilities (Note 13)	995	790
Total Intragovernmental Liabilities (Note 11)	$9,917	$10,892
Accounts Payable	847	817
Loan Guarantees Liabilities (Note 9)	4,678	5,172
Debt Held by the Public (Note 12)	1,542	1,858
Federal Employee and Veterans' Benefits (Note 2)	82	79
Loss Reserves (Note 14)	539	519
Other Governmental Liabilities (Note 13)	1,014	1,199
TOTAL LIABILITIES (Note 11)	$18,619	$20,536
NET POSITION		
Unexpended Appropriations	$53,828	$58,131
Cumulative Results of Operations	38,122	34,527
Total Net Position	91,950	92,658
Total Liabilities and Net Position	$110,569	$113,194

Consolidating Statement of Net Cost
For the Period Ended September 2005 and 2004
(Dollars in millions)

	2005	2004
COSTS:		
Federal Housing Administration		
Intragovernmental	$532	$719
Intragovernmental Earned Revenues	(1,491)	(1,552)
Intragovernmental Net Costs	($959)	($832)
With the Public	$254	($667)
Earned Revenue With the Public	(363)	(250)
Net Costs With the Public	($109)	($917)
Net Program Costs	($1,068)	($1,750)
Government National Mortgage Association		
Intragovernmental		
Intragovernmental Earned Revenues	($457)	($443)
Intragovernmental Net Costs	($457)	($443)
With the Public	$81	$78
Earned Revenues	(329)	(373)
Net Costs With the Public	($248)	($295)
Net Program Costs	($705)	($738)
Section 8		
Intragovernmental	$65	$64
Intragovernmental Earned Revenues		
Intragovernmental Net Costs	$65	$64
With the Public	$23,330	$22,401
Earned Revenues		
Net Costs With the Public	$23,330	$22,401
Net Program Costs	$23,395	$22,465
Low Rent Public Housing Loans and Grants		
Intragovernmental	$176	$189
Intragovernmental Earned Revenues		
Intragovernmental Net Costs	$176	$189
With the Public	$3,425	$3,711
Earned Revenues		
Net Costs With the Public	$3,425	$3,711
Net Program Costs	$3,601	$3,900

(continued)

Operating Subsidies		
Intragovernmental	$12	$16
Intragovernmental Earned Revenues		
Intragovernmental Net Costs	$12	$16
With the Public	$3,555	$3,449
Earned Revenues		
Net Costs With the Public	$3,555	$3,449
Net Program Costs	$3,567	$3,465
Housing for the Elderly and Disabled		
Intragovernmental	$115	$183
Intragovernmental Earned Revenues		
Intragovernmental Net Costs	$115	$183
With the Public	$1,255	$1,116
Earned Revenues	($553)	(616)
Net Costs With the Public	$702	$500
Net Program Costs	$817	$683
Community Development Block Grants		
Intragovernmental	$23	$38
Intragovernmental Earned Revenues		
Intragovernmental Net Costs	$23	$38
With the Public	$5,002	$5,419
Earned Revenues		
Net Costs With the Public	$5,002	$5,419
Net Program Costs	$5,025	$5,457
HOME		
Intragovernmental	$20	$13
Intragovernmental Earned Revenues		
Intragovernmental Net Costs	$20	$13
With the Public	$1,734	$1,612
Earned Revenues		
Net Costs With the Public	$1,734	$1,612
Net Program Costs	$1,754	$1,625
Other		
Intragovernmental	$204	$163
Intragovernmental Earned Revenues	($9)	(5)
Intragovernmental Net Costs	$195	$158
With the Public	$3,580	$3,415
Earned Revenues	($24)	(32)
Net Costs With the Public	$3,556	$3,383
Net Program Costs	$3,751	$3,541
Costs Not Assigned to Programs	$268	$392
Net Cost of Operations	$40,405	$39,040

Consolidated Statement of Changes in Net Position
For the Period Ended September 2005 and 2004
(Dollars in millions)

	2005		2004 Restated	
	Cumulative Results of Operations	Unexpended Appropriations	Cumulative Results of Operations	Unexpended Appropriations
Net Position-Beginning of Period	($34,527)	($58,131)	($30,166)	($64,753)
Adjustments				
Changes in Accounting Principles				
Correction of Errors			5	
Beginning Balances, As Adjusted	($34,527)	($58,131)	($30,161)	($64,753)
Budgetary Financing Sources				
Appropriations Received		(42,637)		(40,569)
Transfers In/Out		127		85
Other Adjustments (Rescissions, etc)		2,206		3,281
Appropriations Used	(44,607)	44,607	(43,859)	43,825
Transfers In/Out Without Reimbursement	384		306	
Other Budgetary Financing Sources			(2)	
Other Financing Sources				
Donations and Forfeitures of Property				
Transfers In/Out Without Reimbursement	304		209	
Imputed Financing From Costs				
Absorbed From Others	(81)		(62)	
Other			2	
Total Financing Sources	($44,000)	$4,303	($43,406)	$6,622
Net Cost of Operations	40,405		39,040	
Net Change	($3,595)	$4,303	($4,366)	$6,622
Ending Balances	($38,122)	($53,828)	($34,527)	($58,131)

Combined Statement of Budgetary Resources
For the Period Ended September 2005 and 2004
(Dollars in millions)

	2005		2004 Restated	
	Budgetary	Non-Budgetary Credit Program Financing Accounts	Budgetary	Non-Budgetary Credit Program Financing Accounts
Budgetary Resources:				
Budget Authority	$43,414	$1,174	$41,223	$3,400
Net Transfer, Current Year Authority	21		10	
Unobligated Balance-Beginning of Year	44,731	4,723	49,888	1,144
Net Transfers, Actual	208		394	
Spending Authority from Offsetting Collections	5,314	11,657	6,800	17,466
Anticipated for Rest of Year				
Adjustments				
Recoveries of Prior Year Obligations	1,996	39	2,096	12
Anticipated Recoveries, Prior Year				
Temporarily Not Available Per PL				
Permanently not available				
Cancellations-Expired and No Year Accts	(130)		(50)	
Enacted Rescissions	(2,274)		(3,094)	
Capital Trans & Debt Redemption	(1,335)	(1,214)	(1,865)	(4,559)
Other Authority Withdrawn	(4,403)		(1,319)	
Total Budgetary Resources	$87,542	$16,379	$94,083	$17,463
Status of Budgetary Resources:				
Obligations Incurred	$44,153	$10,373	$49,352	$12,740
Unobligated Balances Available	7,723	2,662	7,707	2,589
Unobligated Balances Not Available	35,666	3,344	37,024	2,134
Total Status of Budgetary Resources	$87,542	$16,379	$94,083	$17,463
Obligated Balance, Net-Beg of Period	$75,198	$1,108	$80,663	$921
Obligated Balance Transferred, Net				
Obligated Balance, Net - End of Period	68,885	1,191	75,198	1,108
Outlays				
Disbursements	48,465	10,334	52,749	12,420
Collections	(5,308)	(11,740)	(6,828)	(17,345)
Subtotal	$43,157	($1,406)	$45,921	($4,926)
Less: Offsetting Receipts	(483)		(428)	
Net Outlays	$42,674	($1,406)	$45,493	($4,926)

Consolidated Statement of Financing
For the Year Ended September 2005 and 2004
(Dollars in millions)

	2005	2004 Restated
Resources Used to Finance Activities:		
Budgetary Resources Obligated		
Obligations Incurred	$54,526	$62,091
Less: Spending Authority from Offsetting Collections & Recoveries	(19,006)	(26,373)
Obligations Net of Offsetting Collections	$35,520	$35,718
Less: Offsetting Receipts	(483)	(428)
Net Obligations	$35,037	$35,290
Other Resources		
Transfers In/Out Without Reimbursement	(512)	(604)
Imputed Financing from Costs Absorbed by Others	58	63
Other Resources	53	(21)
Net Other Resources Used to Finance Activities	($401)	($562)
Total Resources Used to Finance Activities	$34,636	$34,728
Resources Used to Finance Items Not Part of the Net Cost of Operations		
Change in Budgetary Resources Obligated for Goods Services/Benefits Ordered but not yet Provided	$6,312	$4,921
Resources That Fund Expenses from Prior Periods	(3,162)	(7,548)
Budgetary Offsetting Collections and Receipts Not Affecting Net Cost of Operations	14,262	21,203
Resources Financing Acquisition of Assets	(10,103)	(12,595)
Other Changes to Net Obligated Resources Not Affecting Net Cost of Operations	(501)	71
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	$6,808	$6,052
Total Resources Used to Finance the Net Cost of Operations	$41,444	$40,780

Consolidated Statement of Financing (continued)
For the Year Ended September 2005 and 2004
(Dollars in millions)

Components of Net Cost of Operations Not Requiring/Generating Resources in the Current Period:		
Components Requiring or Generating Resources in Future Periods		
Increase in Annual Leave Liability (Note 22)	$2	$3
Re-estimates of Credit Subsidy Expense	2,131	2,859
Exchange Revenue Receivable from the Public	(563)	(615)
Other	3	(5)
Total Requiring/Generating Resources in Future Periods	$1,573	$2,242
Components Not Requiring/Generating Resources		
Depreciation and Amortization	$15	$14
Revaluation of Assets or Liabilities	(1,338)	(1,433)
Other	(1,289)	(2,563)
Total Components of Net Cost of Operation Not Requiring/Generating Resources	($2,612)	($3,982)
Total Components of Net Cost of Operations Not Requiring/Generating Resources in the Current Period	($1,039)	($1,740)
Net Cost of Operations	$40,405	$39,040

Notes to the Financial Statements September 30, 2005 and 2004

Note 1 – Entity and Mission

The U.S. Department of Housing and Urban Development (HUD) was created in 1965 to (1) provide housing subsidies for low- and moderate-income families, (2) provide grants to states and communities for community development activities, (3) provide direct loans and capital advances for construction and rehabilitation of housing projects for the elderly and persons with disabilities, and (4) promote and enforce fair housing and equal housing opportunity. In addition, HUD insures mortgages for single family and multifamily dwellings, insures loans for home improvements and manufactured homes, and facilitates financing for the purchase or refinancing of millions of American homes.

HUD's major programs are as follows:

The **Federal Housing Administration** (FHA) was established under the National Housing Act of 1934 and became a wholly owned government corporation in 1948 subject to the Government Corporation Control Act, as amended. While FHA was established as a separate federal entity, it was subsequently merged into HUD when it was created in 1965. FHA administers active mortgage insurance programs that are designed to make mortgage financing more accessible to the homebuying public and thereby to develop affordable housing. FHA insures private lenders against loss on mortgages that finance single family homes, multifamily projects, health care facilities, property improvements, and manufactured homes.

The **Government National Mortgage Association** (Ginnie Mae) was created as a Government corporation within HUD to administer mortgage support programs that could not be carried out in the private market. Ginnie Mae guarantees the timely payment of principal and interest on mortgage-backed securities issued by approved private mortgage institutions and backed by pools of mortgages insured or guaranteed by FHA, the Rural Housing Service, the Department of Veterans Affairs, and the HUD Office of Public and Indian Housing (PIH).

The **Section 8 Rental Assistance** programs assist low- and very low-income families in obtaining decent and safe rental housing. HUD makes up the difference between what a low- and very low-income family can afford and the approved rent for an adequate housing unit.

Operating Subsidies are provided to Public Housing Authorities (PHAs) and Tribally Designated Housing Entities to help finance the operations and maintenance costs of their housing projects.

The **Community Development Block Grant** (CDBG) programs provide funds for metropolitan cities, urban counties, and other communities to use for neighborhood revitalization, economic development, and improved community facilities and services. The United States Congress appropriated $2 billion in FY 2002 and $783 million in emergency supplemental appropriations in FY 2001 for the "Community Development Fund" for emergency expenses to respond to the September 11, 2001 terrorist attacks on the United States. Of the amounts appropriated, $111 million was expensed in FY 2005 and $517 million was expensed in FY 2004. Any remaining unobligated balances shall remain available until expended.

The **Low Rent Public Housing Grants** program provides grants to PHAs and Tribally Designated Housing Entities for construction and rehabilitation of low-rent housing. This program is a continuation of the Low Rent Public Housing Loan Program, which pays principal and interest on long-term loans made to PHAs and these entities for construction and rehabilitation of low rent housing.

The **Section 202/811 Supportive Housing for the Elderly and Persons with Disabilities** programs, prior to FY 1992, provided 40-year loans to nonprofit organizations sponsoring rental housing for the elderly or disabled. During FY 1992, the program was converted to a grant program. The grant program provides long-term supportive housing for the elderly (Section 202) and disabled (Section 811).

The **HOME Investment Partnerships** program provides grants to states, local governments, and Indian tribes to implement local housing strategies designed to increase homeownership and affordable housing opportunities for low- and very low-income Americans.

Other Programs not included above consist of smaller programs that provide grant, subsidy funding, and direct loans to support other HUD objectives such as fair housing and equal opportunity, energy conservation, assistance for the homeless, rehabilitation of housing units, and homeownership. These programs comprise approximately 8.6 percent of HUD's consolidated assets and 7.9 percent of HUD's consolidated revenues and financing sources for FY 2005, and 8.8 percent of HUD's consolidated assets and 9.1 percent of HUD's consolidated revenues and financing sources for FY 2004.

Note 2 – Summary of Significant Accounting Policies

A. Basis of Consolidation

The financial statements include all funds and programs for which HUD is responsible. All significant intra-fund balances and transactions have been eliminated in consolidation. Transfer appropriations are consolidated into the financial statements based on an evaluation of their relationship with HUD.

B. Basis of Accounting

The financial statements include the accounts and transactions of the Ginnie Mae, FHA, and HUD's Grant, Subsidy, and Loan programs.

The financial statements are presented in accordance with OMB Circular No. A-136, Financial Reporting Requirements, and in conformance with the Federal Accounting Standards Advisory Board's Statements of Federal Financial Accounting Standards.

The financial statements are presented on the accrual basis of accounting. Under this method, HUD recognizes revenues when earned, and expenses when a liability is incurred, without regard to receipt or payment of cash. Generally, procedures for HUD's major grant and subsidy programs require recipients to request periodic disbursement concurrent with incurring eligible costs.

The Department's disbursement policy permits grantees/recipients to request funds to meet immediate cash needs to reimburse themselves for eligible incurred expenses and eligible expenses expected to be received and paid within three days. HUD's disbursement of funds for these purposes are not considered advance payments, but are viewed as good cash management between the Department and the grantees. In the event it is determined that the grantee/recipient did not disburse the funds within the three day time frame, interest earned must be returned to HUD and deposited into one of Treasury's miscellaneous receipt accounts.

C. Use of Estimates

The preparation of the principal financial statements in conformity with Generally Accepted Accounting Principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

Amounts reported for net loans receivable and related foreclosed property and the loan guarantee liability represent the Department's best estimates based on pertinent information available.

To estimate the allowance for subsidy associated with loans receivable and related to foreclosed property and the liability for loan guarantees, the Department uses cash flow model assumptions associated with loan guarantee cases subject to the Federal Credit Reform Act of 1990, as described in Note 9, to estimate the cash flows associated with future loan performance. To make reasonable projections of future loan performance, the Department develops assumptions based on historical data, current and forecasted program and economic assumptions.

Certain programs have higher risks due to increased chances of fraudulent activities perpetrated against the Department. The Department accounts for these risks through the assumptions used in the liabilities for loan guarantee estimates. HUD develops the assumptions based on historical performance and management's judgments about future loan performance.

D. Credit Reform Accounting

The primary purpose of the Federal Credit Reform Act of 1990, which became effective on October 1, 1991, is to more accurately measure the cost of federal credit programs and to place the cost of such credit programs on a basis equivalent with other federal spending. OMB Circular A-129, Federal Credit Programs, defines a loan guarantee as any guarantee, insurance, or other pledge with respect to the payment of all, or a part of, the principal or interest on any debt obligation of a non-federal borrower (issuer) to a non-federal lender (investor). In the opinion of Ginnie Mae management and HUD's General Counsel, the Federal Credit Reform Act does not apply to Ginnie Mae. Nevertheless, in consultation with OMB, Ginnie Mae has adopted certain credit reform practices.

The Federal Credit Reform Act also establishes the use of the program, financing, general fund receipt, and capital reserve accounts for loan guarantees committed and direct loans obligated after September 30, 1991 (Credit Reform). It also establishes the liquidating account for activity relating to any loan guarantees committed and direct loans obligated before October 1, 1991 (pre-Credit Reform). These accounts are classified as either budgetary or non-budgetary in the Combined Statements of Budgetary Resources. The budgetary accounts include the program, capital reserve, and liquidating accounts. The non-budgetary accounts consist of the credit reform financing accounts.

The program account is a budget account that receives and obligates appropriations to cover the subsidy cost of a direct loan or loan guarantee and disburses the subsidy cost to the financing account. The program account also receives appropriations for administrative expenses. The financing account is a non-budgetary account that records all of the cash flows resulting from Credit Reform direct loans or loan guarantees. It disburses loans, collects repayments and fees, makes claim payments, holds balances, borrows from the U.S. Treasury, earns or pays interest, and receives the subsidy cost payment from the program account.

The general fund receipt account is a budget account used for the receipt of amounts paid from the financing account when there is a negative subsidy from the original estimate or a downward re-estimate. In most cases, the receipt account is a general fund receipt account and amounts are not earmarked for the credit program. They are available for appropriations only in the sense that all general fund receipts are available for appropriations. Any assets in this account are non-entity assets and are offset by intragovernmental liabilities. At the beginning of the following fiscal year, the fund balance in the general fund receipt account is transferred to the U.S. Treasury General Fund. The FHA General Fund receipt account of the General Insurance and Special Risk Insurance funds are in this category.

In order to resolve the different requirements between the Federal Credit Reporting Act of 1990 and the National Affordable Housing Act of 1990, OMB instructed FHA to create the capital reserve account to retain the Mutual Mortgage Insurance/Cooperative Management Housing Insurance negative subsidy and subsequent downward re-estimates. Specifically, the National Affordable Housing Act required that FHA's Mutual Mortgage Insurance fund achieve a Capital Ratio of 2.0 percent by FY 2000. The Capital Ratio is defined as the ratio of economic net worth (current cash plus the present value of all future net cash flows) of this fund to unamortized insurance in force (the unpaid balance of insured mortgages). Therefore, to ensure that the calculated Capital Ratio reflects the actual strength of the Mutual Mortgage Insurance fund, the resources of the capital reserve account, which are considered FHA assets, are included in the calculation of the fund's economic net worth. At the end of FY 1995, FHA met and has since maintained the Capital Ratio requirement. FHA's actuary estimates the September 30, 2005, Capital Ratio at 6.02 percent. The FY 2004 estimated Capital Ratio was 5.53 percent.

The liquidating account is a budget account that records all cash flows to and from FHA resulting from pre-Credit Reform direct loans or loan guarantees. Liquidating account collections in any year are available only for obligations incurred during that year or to repay debt. Unobligated balances remaining in the General Insurance and Special Risk Insurance liquidating funds at year-end are transferred to the U.S. Treasury's General Fund. Consequently, in the event that resources in the General Insurance/Special Risk Insurance liquidating account are otherwise insufficient to cover the payments for obligations or commitments, the Federal Credit Reform Act provides the liquidating account with permanent indefinite authority to cover any resource shortages.

E. Operating Revenue and Financing Sources

HUD finances operations principally through appropriations, collection of premiums and fees on its FHA and Ginnie Mae programs, and interest income on its mortgage notes, loans, and investments portfolio.

Appropriations for Grant and Subsidy Programs

HUD receives both annual and multi-year appropriations, and recognizes those appropriations as revenue when related program expenses are incurred. Accordingly, HUD recognizes grant-related revenue and related expenses as recipients perform under the contracts. HUD recognizes subsidy-related revenue and related expenses when the underlying assistance (e.g., provision of a Section 8 rental unit by a housing owner) is provided.

FHA Unearned Premiums

Premiums charged by FHA for single family mortgage insurance provided by its Mutual Mortgage Insurance and Cooperative Management Housing Insurance Fund include up-front and annual risk based premiums. Pre-credit reform upfront risk-based premiums are recorded as unearned revenue upon collection and are recognized as revenue over the period in which losses and insurance costs are expected to occur. Annual risk-based premiums are recognized as revenue on a straight-line basis throughout the year. FHA's other activities charge periodic insurance premiums over the mortgage insurance term. Premiums on annual installment policies are recognized for the liquidating accounts on a straight-line basis throughout the year.

Premiums associated with Credit Reform loan guarantees are included in the calculation of the liability for loan guarantees, and are not included in the unearned premium amount reported on the Balance Sheet, since these guarantees represent the net present value of future cash flows associated with those insurance portfolios.

Ginnie Mae Fees

Fees received for Ginnie Mae's guaranty of mortgage-backed securities are recognized as earned on an accrual basis. Commitment fees represent income that Ginnie Mae earns for providing approved issuers with authority to pool mortgages into Ginnie Mae mortgage-backed securities. The authority Ginnie Mae provides issuers expires 12 months from issuance for single family issuers and 24 months from issuance for multifamily issuers. Ginnie Mae receives commitment fees as issuers request commitment authority and recognizes the commitment fees as earned as issuers use their commitment authority, with the balance deferred until earned or expired, whichever occurs first. Fees from expired commitment authority are not returned to issuers.

F. Appropriations and Moneys Received from Other HUD Programs

The National Housing Act of 1990, as amended, provides for appropriations from Congress to finance the operations of the General Insurance and Special Risk Insurance funds. For Credit Reform loan guarantees, appropriations to these funds are provided at the beginning of each fiscal year to cover estimated losses on insured loans during the year. For pre-Credit Reform loan guarantees, FHA has permanent indefinite appropriation authority to finance any shortages of resources needed for operations.

Monies received from other HUD programs, such as interest subsidies and rent supplements, are recorded as revenue for the liquidating accounts when services are rendered. Monies received for the financing accounts are recorded as additions to the liability for loan guarantees or the Allowance for Subsidy when collected.

G. Investments

HUD limits its investments, principally comprised of investments by FHA's Mutual Mortgage Insurance/ Cooperative Management Housing Insurance Fund and by Ginnie Mae, to non-marketable market-based Treasury interest-bearing obligations (i.e., investments not sold in public markets). The market value and interest rates established for such investments are the same as those for similar Treasury issues, which are publicly marketed.

HUD's investment decisions are limited by Treasury policy which: (1) only allows investment in Treasury notes, bills, and bonds; and (2) prohibits HUD from engaging in practices that result in "windfall" gains and profits, such as security trading and full scale restructuring of portfolios, in order to take advantage of interest rate fluctuations. FHA's normal policy is to hold investments in U.S. Government securities to maturity. However, in certain circumstances, FHA may have to liquidate its U.S. Government securities before maturity to finance claim payments.

HUD reports investments in U.S. Government securities at amortized cost. Premiums or discounts are amortized into interest income over the term of the investment. HUD intends to hold investments to maturity, unless needed for operations. No provision is made to record unrealized gains or losses on these securities because, in the majority of cases, they are held to maturity.

The Departments of Veterans Affairs and Housing and Urban Development Appropriations Act of 1999 and Section 601 of the Independent Agencies Act of 1999 provide FHA with new flexibility in reforming its single family claims and property disposition activities. In accordance with these Acts, FHA implemented the Accelerated Claims Disposition Demonstration Program (the Section 601 program) to shorten the claim filing process, obtain higher recoveries from its defaulted guaranteed loans, and support the Office of Housing's mission of keeping homeowners in their home. To achieve these objectives, FHA transfers assigned mortgage notes to private sector entities in exchange for cash and equity interest. The servicing and disposition of the mortgage notes are performed by the private sector entities whose primary mission is dedicated to these types of activities.

With the transfer of assigned mortgage notes under the Section 601 program, FHA obtains ownership interest in the private sector entities. This level of ownership interest enables FHA to exercise significant influence over the operating and financial policies of the entities. Accordingly, to comply with the requirement of Opinion Number 18 issued by the Accounting Principles Board, FHA uses the equity method of accounting to measure the value of its investments in these entities. The equity method of accounting requires FHA to record its investments in the entities at cost initially. Periodically, the carrying amount of the investments is adjusted for cash distributions to FHA and for FHA's share of the entities' earnings or losses.

H. Credit Program Receivables and Related Foreclosed Property

HUD finances mortgages and provides loans to support construction and rehabilitation of low rent housing, principally for the elderly and disabled under the Section 202/811 program. Prior to April 1996, mortgages were also assigned to HUD through FHA claims settlement (i.e., mortgage notes assigned). Single family mortgages were assigned to FHA when the mortgagor defaulted due to certain "temporary hardship" conditions beyond the control of the mortgagor, and when, in management's judgment, it was likely that the mortgage could be brought current in the future. FHA's loans receivable include mortgage notes assigned, also described as Secretary-held notes, and purchase money mortgages. Under the requirements of the Federal Credit Reporting Act, purchase money mortgages notes are considered to be direct loans while mortgage notes assigned notes are considered to be defaulted guaranteed loans. The purchase money mortgages loans are generated from the sales on credit of FHA's foreclosed properties to qualified nonprofit organizations. The mortgage notes assigned are created when FHA pays the lenders for claims on defaulted guaranteed loans and takes assignment of the defaulted loans for direct collections. In addition, multifamily mortgages are assigned to FHA when lenders file mortgage insurance claims for defaulted notes.

Credit program receivables for direct loan programs and defaulted guaranteed loans assigned for direct collection are valued differently based on the direct loan obligation or loan guarantee commitment date. These valuations are in accordance with the Federal Credit Reform Act of 1990 and Statement of Federal Financial Accounting Standards Number 2, "Accounting for Direct Loans and Loan Guarantees," as amended by Statements of Federal Financial Accounting Standards Number 18. Those obligated or committed on or after October 1, 1991 (post-Credit Reform) are valued at the net present value of expected cash flows from the related receivables.

Credit program receivables resulting from obligations or commitments prior to October 1, 1991 (pre-Credit Reform) are recorded at the lower of cost or fair value (net realizable value). Fair value is estimated based on the prevailing market interest rates at the date of mortgage assignment. When fair value is less than cost, discounts are recorded and amortized to interest income over the remaining terms of the mortgages or upon sale of the mortgages. Interest is recognized as income when earned. However, when full collection of principal is considered doubtful, the accrual of interest income is suspended and receipts (both interest and principal) are recorded as collections of principal. Pre-Credit Reform loans are reported net of allowance for loss and any unamortized discount. The estimate for the allowance on credit program receivables is based on historical loss rates and recovery rates resulting from asset sales and property recovery rates, net of cost of sales.

Foreclosed property acquired as a result of defaults of loans obligated or loan guarantees committed on or after October 1, 1991, is valued at the net present value of the projected cash flows associated with the property. Foreclosed property acquired as a result in defaulted loans obligated or loan guarantees committed prior to 1992 is valued at net realizable value. The estimate for the allowance for loss related to the net realizable value of foreclosed property is based on historical loss rates and recovery rates resulting from property sales, net of cost of sales.

I. Borrowings

As further discussed in Note 12, several of HUD's programs have the authority to borrow funds from the U.S. Treasury from program operations. These borrowings, representing unpaid principal balances and future accrued interest, are reported as debt in HUD's consolidated financial statements. The PIH Low Rent Public Housing Loan Program and the Housing for the Elderly or Handicapped fund were financed through borrowings from the Federal Financing Bank or the U.S. Treasury prior to the Department's conversion of these programs to grant programs. The Department also borrowed funds from the private sector to assist in the construction and rehabilitation of low rent housing projects under the PIH Low Rent Public Housing Loan Program. Repayments of these long-term borrowings have terms up to 40 years.

In accordance with Credit Reform accounting, FHA also borrows from the U.S. Treasury when cash is needed in its financing accounts. Usually, the need for cash arises when FHA has to transfer the negative credit subsidy amount related to new loan disbursements, and existing loan modifications from the financing accounts to the general fund receipts account (for cases in General Insurance/Special Risk Insurance funds) or the liquidating account (for cases in Mutual Mortgage Insurance/Cooperative Management Housing Insurance funds). In some instances, borrowings are also needed to transfer the credit subsidy related to downward re-estimates from the General Insurance/Special Risk Insurance financing account to the corresponding receipt account or when available cash is less than claim payments due.

J. Liability for Loan Guarantees

The potential future losses related to FHA's central business of providing mortgage insurance are accounted for as Loan Guarantee Liability in the consolidated balance sheets. As required by Statement of Federal Financial Accounting Standards Number 2, the Loan Guarantee Liability includes the Credit Reform-related Liabilities for Loan Guarantees and the Loan Loss Reserve.

The Liabilities for Loan Guarantees and the Loan Loss Reserve are calculated as the present value of anticipated cash outflows for defaults, such as claim payments, premium refunds, property expense for on-hand properties, and sale expense for sold properties, less anticipated cash inflows such as premium receipts, proceeds from asset sales and principal and interest on Secretary-held notes acquired from FHA's claim settlements of defaulted mortgages or pursuant to Section 221(g)(4) of the National Housing Act.

HUD records its loan loss reserves for its mortgage insurance programs operated through FHA and its financial guaranty programs operated by Ginnie Mae. FHA loss reserves are recorded for the net present value of estimated future cash flows associated with FHA-insured mortgage loans endorsed before FY 1992. Ginnie Mae establishes reserves for actual and probable defaults of issuers of Ginnie Mae-guaranteed mortgage-backed securities. Such reserves disclosed in the consolidated financial statements are based on management's judgment about historical claim and loss information and current and projected economic factors.

K. Full Cost Reporting

Statement of Federal Financial Accounting Standards Number 4 requires that full costing of program outputs be included in federal agency financial statements. Full cost reporting includes direct, indirect, and inter-entity costs. For purposes of the consolidated Department financial statements, HUD identified each responsible segment's share of the program costs or resources provided by HUD or other federal agencies.

These costs are treated as imputed cost for the Statement of Net Cost, and imputed financing for the Statement of Changes in Net Position and the Statement of Financing.

L. Accrued Unfunded Leave and Federal Employees Compensation Act Liabilities

Annual leave and compensatory time are accrued as earned and the liability is reduced as leave is taken. The liability at year-end reflects cumulative leave earned but not taken, priced at current wage rates. Earned leave deferred to future periods is to be funded by future appropriations. HUD offsets this unfunded liability by recording future financing sources in the Net Position section of its Consolidated Balance Sheet. Sick leave and other types of leave are expensed as taken.

HUD also accrues the portion of the estimated liability for disability benefits assigned to the agency under the Federal Employees' Compensation Act, administered and determined by the Department of Labor. The liability, based on the net present value of estimated future payments based on a study conducted by the Department of Labor, was $82 million as of September 30, 2005, and $79 million as of September 30, 2004. Future payments on this liability are to be funded by future appropriations. HUD offsets this unfunded liability by recording future financing sources.

M. Retirement Plans

The majority of HUD's employees participate in either the Civil Service Retirement System or the Federal Employees Retirement System. The latter program went into effect pursuant to Public Law 99-335 on January 1, 1987. Most employees hired after December 31, 1983, are automatically covered by the Federal Employees Retirement System and Social Security. Employees hired before January 1, 1984, can elect to either join this program and Social Security or remain in the Civil Service Retirement System. HUD expenses its contributions to the retirement plans.

A primary feature of the Federal Employees Retirement System is that it offers a savings plan whereby HUD automatically contributes 1 percent of pay and matches any employee contribution up to an additional 4 percent of pay. Under the Civil Service Retirement System, employees can contribute up to 15 percent of their pay to the savings plan, but there is no corresponding matching by HUD. Although HUD funds a portion of the benefits under the Federal Employees Retirement System relating to its employees and makes the necessary withholdings from them, it has no liability for future payments to employees under these plans, nor does it report any retirement plan assets, Federal Employees' Compensation Act assets, accumulated plan benefits, or unfunded liabilities applicable to its employees' retirement plans. These amounts are reported by the Office of Personnel Management and are not allocated to the individual employers. HUD's matching contribution to these retirement plans during FY 2005 and FY 2004 was $79 million and $77 million, respectively.

N. Federal Employee and Veterans' Benefit

The Department's Federal Employee and Veterans' benefit expenses totaled approximately $137 million for FY 2005; this amount includes $36 million to be funded by the Office of Personnel Management. Amounts funded by the Office of Personnel Management are charged to expense with a corresponding amount considered as an imputed financing source in the Statement of Changes in Net Position.

O. Financial Accounting Standards Board Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees

The Financial Accounting Standards Board Interpretation Number 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, is an interpretation of Financial Accounting Standards Board Statements Numbers 5, 57, and 107, and Rescission of Interpretation No. 34, in November 2002. Interpretation Number 45 clarifies the requirements of Statement Number 5, Accounting for Contingencies, relating to the guarantor's accounting for, and disclosure of, the issuance of certain types of guarantees. Interpretation Number 45 requires that upon issuance of a guarantee, the entity (i.e., the guarantor) must recognize a liability for the fair value of the obligation it assumes under that guarantee. The disclosure provisions of Interpretation Number 45 are effective for financial statements that end after December 15, 2002. These provisions for initial recognition and measurement are to be applied on a prospective basis only to guarantees issued or modified after December 31, 2002. The guarantor's previous accounting for guarantees that were issued before the date of Interpretation 45's initial application may not be revised or restated to reflect the effect of the recognition and measurement provisions of this Interpretation. Ginnie Mae has completed an evaluation of its guarantees for disclosures required by Interpretation 45, and have disclosed an asset and liability of $382.3 million (i.e., Other Assets and Other Liabilities). There is no impact of adopting this interpretation on the net financial position.

P. Re-estimate of Obligated Balance for Section 236

HUD's Section 236 Interest Reduction Program was established under the National Housing Act (Public Law 90-448), enacted in 1968 for the purpose of providing an incentive to develop rental housing for low- and moderate-income households. The incentive is a HUD subsidy for the difference between the monthly payment for principal, interest, and mortgage insurance premiums on the outstanding mortgage at the market rate of interest and the monthly payments that are required under a mortgage bearing an interest rate of one percent. This makes HUD liable to the mortgage lender/servicer for the balance of the interest due. Generally, mortgages were originated with a term of 40 years, with certain program provisions that could result in early termination of the Interest Reduction Program agreement, or payment deferrals and program term extensions up to a period of 50 years. New program activity was terminated in the late 1970s and HUD maintained the remaining program liability in its official accounting system as the cumulative remaining estimated obligation amount. HUD has permanent indefinite contract authority to cover the remaining obligations under this program. In FY 2004, the Office of Inspector General reported internal control deficiencies in the Section 236 Interest Reduction Program that called the remaining estimated obligation balance into question. To address this reportable condition, HUD's Office of the CFO contracted for a 100 percent reconciliation and reconstruction of records for the Section 236 Interest Reduction Program in FY 2005, with improved integration and automation of the business and accounting processes to maintain accurate program balances going forward. This effort reconciled information on over 3,000 Interest Reduction Program agreements and determined a revised estimated cumulative remaining obligation balance of $5.1 billion. HUD requested that OMB apportion $757 million in additional permanent indefinite authority to fully cover the revised estimated remaining obligation balance, which is reflected in the Statement of Budgetary Resources as a current year obligation. There are 51 projects where, due to missing documentation or ambiguous terms, the contractor could not yet determine if the term of the Interest Reduction Program agreement was 40 or 50 years. To be conservative, HUD assumed that these agreements will be valid for 50 years from the date they were executed. As a result, there is a potential $352 million overstatement of the $5.1 billion cumulative obligation balance for the Section 236 Interest Reduction Program if it is subsequently found that the program agreements for all 51 projects were actually valid for only 40 years from the date they were executed.

Q. Emergency Relief Efforts for Hurricane Katrina

Ginnie Mae guarantees advance payments of principal and interest on mortgage-backed securities when the issuer of the pooled mortgages behind these securities defaults. Ginnie Mae files the claims for loans defaulted within the defaulted issuers portfolio to FHA, the Department of Veterans Affairs, or the Rural

Housing Service. Due to Hurricane Katrina, the pool income stream has been disrupted from destruction of the collateral, displacement of the FHA or Department of Veterans Affairs loan borrowers, and the loss of borrower employment. Ginnie Mae has determined that there are about $6.5 billion of mortgages underlying its Mortgage-Backed Securities guaranteed program in the affected region. Most Ginnie Mae issuers in the affected region are currently able to advance funds when required. Ginnie Mae believes the financial risk to the reserves to be limited, and has identified approximately $500 million in securities portfolios that may be at risk of default. Past experience has shown that approximately one percent of defaulted portfolios are not covered by FHA insurance. Therefore, it is adding additional funds to the Reserve for Loss. Ginnie Mae has estimated $5 million to cover the identified potential risk and an additional $5 million to cover unidentified financial risks. This would bring its total Reserve for Loss to $538 million.

The Department will provide transitional housing assistance to displaced public housing residents, displaced Section 8 participants, displaced families from other HUD assisted programs, and individuals who were homeless in the disaster affected area prior to Katrina.

R. Restatements

In FY 2005, HUD restated its FY 2004 Balance Sheet and Statement of Changes in Net Position for the effect of incorrect application of Statement of Federal Financial Accounting Standard Number 7, issued in 1998. The incorrect application resulted in an overstatement of liabilities and understatement of net position in the amount of $4.2 billion. This amount represented cumulative activity reported as a liability payable to Treasury from the Housing for the Elderly and Disabled program, a loan guarantee liquidating account. In FY 2001, in conjunction with the revisions to central agency guidance on accounting for federal credit programs, HUD began its application of Statement of Federal Financial Accounting Standards Number 7 to the Housing for the Elderly and Disabled program, but delayed reclassification of the liability to Treasury until the guidance was completed in July 2004. As a result, in FY 2005, $4.2 billion was reclassified from other intragovernmental liabilities to cumulative results of operations. Prior to the issuance of Statement of Federal Financial Accounting Standards Number 7, central agency guidance recommended that the cumulative activity in liquidating accounts be treated as a liability to Treasury.

In the Department’s Combined Statement of Budgetary Resources for FY 2004, the Credit Subsidy Amount of $415 million transferred by Ginnie Mae to the general fund receipt account was reported as Spending Authority from Offsetting Collections. As requested by OMB, the Credit Subsidy amount was reclassified from an offsetting collection to a non-expenditure transfer and, unlike Credit Reform, the Ginnie Mae Receipt Account is not swept to the U.S. Treasury General Fund at the end of each fiscal year. These funds are maintained on Ginnie Mae’s books as a cash reserve. Ginnie Mae also received a payment of $10 million from the general fund receipt account for administrative expenses necessary to carry out the guaranteed Mortgage-Backed Securities Program, resulting in a net increase of $405 million in net outlays reported on HUD's restated financial statements. OMB Circular A-11, Preparation, Submission and Execution of the Budget, requires that cash transfers to the general fund receipt account be recorded as non-expenditure transfers and should not offset the amount of gross outlays reported on the Statement of Budgetary Resources. The adjustment of $405 million on the Net Cost of Operations reported on the Statement of Financing was not impacted since the adjustment of $405 million previously reported as an offsetting collection in the Statement of Financing was reclassified as Other Resources in HUD’s restated financial statements.

Note 3 – Fund Balance with the U.S. Treasury

The U.S. Treasury, which, in effect, maintains HUD's bank accounts, processes substantially all of HUD's receipts and disbursements. HUD's fund balances with the U.S. Treasury as of September 30, 2005 and 2004, were as follows (dollars in millions):

Description	2005	2004
Revolving Funds	$ 12,410	$ 10,782
Appropriated Funds	53,723	58,092
Trust Funds	5	5
Other	1,362	768
Total - Fund Balance	$ 67,500	$ 69,647

The Department's Fund Balance with Treasury includes receipt accounts established under current Federal Credit Reform legislation and cash collections deposited in restricted accounts that cannot be used by HUD for its programmatic needs. These designated funds established by the Department of Treasury are classified as suspense and/or deposit funds and consist of accounts receivable balances due from the public. A Statement of Budgetary Resources is not prepared for these funds since any cash remittances received by the Department are not defined as a budgetary resource.

In addition to fund balance, contract and investment authority are also a part of HUD's funding sources. Contract authority permits an agency to incur obligations in advance of an appropriation, offsetting collections, or receipts to make outlays to liquidate the obligations. HUD has permanent indefinite contract authority. Since federal securities are considered the equivalent of cash for budget purposes, investments in them are treated as a change in the mix of assets held, rather than as a purchase of assets.

HUD's fund balances with U.S. Treasury as reflected in the entity's general ledger as of September 30, 2005, were as follows (dollars in millions):

Status of Resources

Description	Unobligated Available	Unobligated Unavailable	Obligated Not Yet Disbursed	Unfilled Customer Orders	Status of Total Resources	Fund Balance	Other Authority	Total Resources
FHA	$ 2,726	$ 26,766	$ 2,330	$ (313)	$ 31,509	$ 9,231	$ 22,278	$ 31,509
Ginnie Mae	-	11,579	121	(78)	11,622	3,711	7,911	11,622
Section 8 Rental Assistance	2,035	76	21,819	-	23,930	10,689	13,241	23,930
CDBG	1,183	36	10,659	-	11,878	11,878	-	11,878
HOME	318	-	5,557	-	5,875	5,875	-	5,875
Operating Subsidies	-	2	873	-	875	875	-	875
Public Housing Loans and Grants	384	17	10,421	-	10,822	8,683	2,139	10,822
Housing for the Elderly & Disabled	1,320	17	5,530	-	6,867	6,867	-	6,867
Section 235/236	257	240	6,818	-	7,315	367	6,948	7,315
All Other	2,162	276	6,367	(27)	8,778	8,761	17	8,778
Total	$ 10,385	$ 39,009	$ 70,495	$ (418)	$ 119,471	$ 66,937	$ 52,534	$ 119,471

Status of Resources Covered by Fund Balance

Description	Unobligated Available	Unobligated Unavailable	Obligated Not Yet Disbursed	Unfilled Customer Orders	Fund Balance	Suspense, Deposit and Receipt Accounts	Total Fund Balance
FHA	$ 2,726	$ 4,488	$ 2,330	$ (313)	$ 9,231	$ 474	$ 9,705
Ginnie Mae	-	3,668	121	(78)	3,711	-	3,711
Section 8 Rental Assistance	697	-	9,992		10,689	12	10,701
CDBG	1,183	36	10,659		11,878	-	11,878
HOME	318	-	5,557		5,875	-	5,875
Operating Subsidies	-	2	873		875	-	875
Public Housing Loans and Grants	384	17	8,282		8,683	-	8,683
Housing for the Elderly & Disabled	1,320	17	5,530		6,867	-	6,867
Section 235/236	1	10	356		367	-	367
All Other	2,162	270	6,356	(27)	8,761	77	8,838
Total	$ 8,791	$ 8,508	$ 50,056	$ (418)	$ 66,937	$ 563	$ 67,500

Status of Resources Covered by Other Authority

Description	Unobligated Available	Unobligated Unavailable	Obligated Not Yet Disbursed	Unfilled Customer Orders	Permanent Indefinite Authority	Investment Authority
FHA		$ 22,278				$ 22,278
Ginnie Mae		7,911				7,911
Section 8 Rental Assistance	$ 1,338	76	$ 11,827		$ 13,241	
Public Housing Loans and Grants	-	-	2,139		2,139	
Section 235/236	256	230	6,462		6,948	
All Other	-	6	11		17	
Total	$ 1,594	$ 30,501	$ 20,439	$ -	$ 22,345	$ 30,189

HUD's fund balances with U.S. Treasury as reflected in the entity's general ledger as of September 30, 2004, were as follows (dollars in millions):

Status of Resources

Description	Unobligated Available	Unobligated Unavailable	Obligated Not Yet Disbursed	Unfilled Customer Orders	Status of Total Resources	Fund Balance	Other Authority	Total Resources
FHA	$ 2,738	$ 25,848	$ 2,255	$ (387)	$ 30,454	$ 7,479	$ 22,975	$ 30,454
Ginnie Mae	-	10,841	120	(84)	10,877	3,355	7,522	10,877
Section 8 Rental Assistance	1,563	691	26,383	-	28,637	12,866	15,771	28,637
CDBG	1,307	39	10,693	-	12,039	12,039	-	12,039
HOME	444	12	5,247	-	5,703	5,703	-	5,703
Operating Subsidies	2	1	2,007	-	2,010	2,010	-	2,010
Public Housing Loans and Grants	390	7	11,139	-	11,536	8,788	2,748	11,536
Housing for the Elderly and Disabled	1,619	46	5,496	-	7,161	7,161	-	7,161
Section 235/236	40	1,381	6,467	-	7,888	351	7,537	7,888
All Other	2,192	293	7,002	(32)	9,455	9,428	27	9,455
Total	$ 10,295	$ 39,159	$ 76,809	$ (503)	$ 125,760	$ 69,180	$ 56,580	$ 125,760

Status of Resources Covered by Fund Balance

Description	Unobligated Available	Unobligated Unavailable	Obligated Not Yet Disbursed	Unfilled Customer Orders	Fund Balance	Suspense, Deposit and Receipt Accounts	Total Fund Balance
FHA	$ 2,738	$ 2,873	$ 2,255	$ (387)	$ 7,479	$ 419	$ 7,898
Ginnie Mae	-	3,319	120	(84)	3,355	-	3,355
Section 8 Rental Assistance	-	-	12,866	-	12,866	23	12,889
CDBG	1,307	39	10,693		12,039		12,039
HOME	444	12	5,247		5,703		5,703
Operating Subsidies	2	1	2,007		2,010		2,010
Public Housing Loans and Grants	390	7	8,391		8,788	-	8,788
Housing for the Elderly and Disabled	1,619	46	5,496		7,161		7,161
Section 235/236	1	6	344		351	-	351
All Other	2,192	293	6,975	(32)	9,428	25	9,453
Total	$ 8,693	$ 6,596	$ 54,394	$ (503)	$ 69,180	$ 467	$ 69,647

Status of Resources Covered by Other Authority

Description	Unobligated Available	Unobligated Unavailable	Obligated Not Yet Disbursed	Unfilled Customer Orders	Permanent Indefinite Authority	Investment Authority
FHA	-	$ 22,975	-	-		$ 22,975
Ginnie Mae	-	7,522	-	-		7,522
Section 8 Rental Assistance	$ 1,563	691	$ 13,517	-	$ 15,771	
Public Housing Loans and Grants	-	-	2,748	-	2,748	
Section 235/236	39	1,375	6,123	-	7,537	
All Other	-	-	27	-	27	
Total	$ 1,602	$ 32,563	$ 22,415	$ -	$ 26,083	$ 30,497

An immaterial difference exists between HUD's recorded Fund Balances with the U.S. Treasury and the U.S. Department of Treasury's records. It is the Department's practice to adjust its records to agree with

Treasury's balances at the end of the fiscal year. The adjustments are reversed at the beginning of the following fiscal year.

Note 4 – Commitments Under HUD's Grant, Subsidy, and Loan Programs

A. Contractual Commitments

HUD has entered into extensive long-term contractual commitments under its various grant, subsidy, and loan programs. These commitments consist of legally binding agreements the Department has entered into to provide grants, subsidies, or loans. Commitments become liabilities when all actions required for payment under an agreement have occurred. The mechanism for funding subsidy commitments generally differs depending on whether the agreements were entered into before or after 1988.

Prior to FY 1988, HUD's subsidy programs, primarily the Section 8 program and the Section 235/236 programs, operated under contract authority. Each year, Congress provided HUD the authority to enter into multi-year contracts within annual and total contract limitation ceilings. HUD then drew on, and continues to draw on, permanent indefinite appropriations to fund the current year's portion of those multi-year contracts. Because of the duration of these contracts (up to 40 years), significant authority exists to draw on the permanent indefinite appropriations. Beginning in FY 1988, the Section 8 and the Section 235/236 programs began operating under multi-year budget authority whereby the Congress appropriates the funds "upfront" for the entire contract term in the initial year.

As shown below, appropriations to fund a substantial portion of these commitments will be provided through permanent indefinite authority. These commitments relate primarily to the Section 8 program, and the Section 235/236 rental assistance and interest reduction programs, and are explained in greater detail below.

HUD's commitment balances are based on the amount of unliquidated obligations recorded in HUD's accounting records with no provision for changes in future eligibility, and thus are equal to the maximum amounts available under existing agreements and contracts. Unexpended appropriations and cumulative results of operations shown in the Consolidated Balance Sheet comprise funds in the U.S. Treasury available to fund existing commitments that were provided through "upfront" appropriations, and also include permanent indefinite appropriations received in excess of amounts used to fund the pre-1988 subsidy contracts and offsetting collections.

Prior to FY 2004, the Department did not disclose the amount of permanent indefinite authority required to meet its obligations under the PIH Low Rent Public Housing Loan Fund. The Department's obligations reported on the Statement of Budgetary Resources for this program are the result of liabilities assumed by the agency in repayment of borrowings on behalf of PHAs and Indian housing agencies authorized by Public Law 99-272. The amount of funding required for the repayment of principal and interest are financed by the Debt Service Fund and covered by the amount of permanent indefinite appropriations not to exceed $7.2 billion authorized by the Secretary of the Treasury. These balances in HUD's budget authority were disclosed as a reconciling item between the amount of unexpended appropriations reported in the Consolidated Statement of Financial Position and the obligated balances reported in the Consolidated Statement of Budgetary Resources in prior financial statement audits. Congress converted the PIH Low Rent and Homeownership loan programs to grant programs in 1986.

FHA enters into long-term contracts for both program and administrative services. FHA funds these contractual obligations through appropriations, permanent indefinite authority, and offsetting collections.

The appropriated funds are primarily used to support administrative contract expenses, while the permanent indefinite authority and the offsetting collections are used for program services.

The following shows HUD's obligations and contractual commitments under its grant, subsidy, and loan programs as of September 30, 2005 (dollars in millions):

	Commitments Funded Through			
Programs	Unexpended Appropriations	Permanent Indefinite or Investment Authority	Offsetting Collection	Undelivered Orders - Obligations, Unpaid
FHA	$ 188	$ 364	$ 571	$ 1,123
Ginnie Mae	-	-	-	-
Section 8 Rental Assistance	9,989	11,827		21,816
Community Development Block Grants	10,635	-	-	10,635
HOME Investment Partnerships Program	5,546	-	-	5,546
Operating Subsidies	759	-	-	759
Low Rent Public Housing Grants and Loans	8,129	2,139		10,268
Housing for Elderly and Disabled	5,480	-	-	5,480
Section 235/236	356	6,462	-	6,818
All Other	6,172	11	97	6,280
Total	$ 47,254	$ 20,803	$ 668	$ 68,725

Of the total Section 8 Rental Assistance contractual commitments as of September 30, 2005**,** $18.2 billion relates to project-based commitments, and $3.6 billion relates to tenant-based commitments.

The following shows HUD's obligations and contractual commitments under its grant, subsidy, and loan programs as of September 30, 2004 (dollars in millions):

	Commitments Funded Through				
Programs	Unexpended Appropriations	Permanent Indefinite or Investment Authority	Offsetting Collection	Investments in Federal Securities	Undelivered Orders - Obligations, Unpaid
FHA	$ 169	$ 368	$ 520	$ -	$ 1,057
Ginnie Mae	-	-	-	-	-
Section 8 Rental Assistance	12,854	13,517	-	-	26,371
Community Development Block Grants	10,671	-	-	-	10,671
HOME Investment Partnerships Program	5,237	-	-	-	5,237
Operating Subsidies	1,873	-	-	-	1,873
Low Rent Public Housing Grants and Loans	8,215	2,747	-	-	10,962
Housing for Elderly and Disabled	5,411	-	-	-	5,411
Section 235/236	342	6,123	-	-	6,465
All Other	6,786	27	108	-	6,921
Total	$ 51,558	$ 22,782	$ 628	$ -	$ 74,968

Of the total Section 8 Rental Assistance contractual commitments as of September 30, 2004**,** $20.7 billion relates to project-based commitments, and $5.6 billion relates to tenant-based commitments. With the exception of the Housing for the Elderly and Disabled and Low Rent Public Housing Loan Programs (which have been converted to grant programs), Section 235/236, and a portion of "all other" programs, HUD management expects all of the above programs to continue to incur new commitments under authority granted by Congress in future years. However, estimated future commitments under such new authority are not included in the amounts above.

B. Administrative Commitments

In addition to the above contractual commitments, HUD has entered into administrative commitments, which are reservations of funds for specific projects (including those for which a contract has not yet been executed) to obligate all or part of those funds. Administrative commitments become contractual commitments upon contract execution.

The following shows HUD's administrative commitments as of September 30, 2005 (dollars in millions):

	Administrative Commitments Funded Through			
Programs	Unexpended Appropriations	Permanent Indefinite Appropriations	Offsetting Collections	Total Reservations
Section 8 Rental Assistance Project-Based	$ 17	$ 22	-	$ 39
Section 8 Rental Assistance Tenant-Based	-	1	-	1
Community Development Block Grants	1,001	-	-	1,001
HOME Investment Partnerships Program	277	-	-	277
Low Rent Public Housing Grants and Loans	148	-	-	148
Housing for Elderly and Disabled	415	-	-	415
All Other	668	12	$ 4	684
Total	$ 2,526	$ 35	$ 4	$ 2,565

The following shows HUD's administrative commitments as of September 30, 2004 (dollars in millions):

	Administrative Commitments Funded Through			
Programs	Unexpended Appropriations	Permanent Indefinite Appropriations	Offsetting Collections	Total Reservations
Section 8 Rental Assistance Project-Based	-	$ 113	-	$ 113
Section 8 Rental Assistance Tenant-Based	-	24	-	24
Community Development Block Grants	$ 1,108	-	-	1,108
HOME Investment Partnerships Program	416	-	-	416
Low Rent Public Housing Grants and Loans	148	-	-	148
Housing for Elderly and Disabled	618	-	-	618
All Other	507	$ 24	$ 6	537
Total	$ 2,797	$ 161	$ 6	$ 2,964

Note 5 – Investments

U.S. Government securities are non-marketable intragovernmental securities. Interest rates are established by the U.S. Treasury and during FY 2005 ranged from 0.88 percent to 13.88 percent. During FY 2004, interest rates ranged from 1.28 percent to 12.84 percent. The amortized cost and estimated market value of investments in debt securities as of September 30, 2005 and 2004, were as follows (dollars in millions):

	Cost	Par Value	Unamortized Premium (Discount)	Accrued Interest	Net Investments	Unamortized Gain	Market Value
FY 2005	$ 30,406	$ 30,595	$ (189)	$ 309	$ 30,715	$ 511	$ 31,226
FY 2004	$ 30,669	$ 30,887	$ (165)	$ 307	$ 31,029	$ 1,150	$ 32,179

Investments in Private Sector Entities

These investments in private sector entities are the result of FHA's participation in the Accelerated Claims Disposition Demonstration program in FY 2005 and 2004, as discussed in Note 2. The following table presents financial data on FHA's investments in private sector entities as of September 30 (dollars in millions):

	Beginning Balance	New Acquisitions	Share of Earnings or Losses	Return of Investments	Other Adjustments	Ending Balance
FY 2005	$ 122	$ 252	$ 58	$ (231)	$ -	$ 201
FY 2004	$ 123	$ 123	$ 62	$ (185)	$ (1)	$ 122

The condensed, audited financial information related to these private sector entities as of June 30, 2005, and for the period from inception to June 30, 2004, is summarized below (dollars in millions):

	2005	2004
Total assets, primarily mortgage loans	$ 499	$ 349
Liabilities	$ 3	$ 2
Partners' capital	496	347
Total liabilities and partners' capital	$ 499	$ 349
Revenues	$ 235	$ 62
Expenses	(31)	(11)
Net Income	$ 204	$ 51

Note 6 – Entity and Non-Entity Assets

Non-entity assets consist of assets that belong to other entities but are included in the Department's consolidated financial statements and are offset by various liabilities to accurately reflect HUD's net position. The Department's non-entity assets principally consist of: (1) U.S. deposit of negative credit subsidy in the General Insurance/Special Risk Insurance general fund receipt account, (2) escrow monies collected by FHA that are either deposited at the U.S. Treasury, minority-owned banks or invested in U.S. Treasury securities, and (3) cash remittances from Section 8 bond refundings deposited in the General Fund of the Treasury.

The following shows HUD's assets as of September 30, 2005 and 2004 (dollars in millions):

Description	2005 Entity	2005 Non-Entity	2005 Total	2004 Entity	2004 Non-Entity	2004 Total
Intragovernmental						
Fund Balance with Treasury (Note 3)	$ 66,118	$ 1,382	$ 67,500	$ 68,793	$ 854	$ 69,647
Investments (Note 5)	30,711	4	30,715	31,025	4	31,029
Accounts Receivable (net) (Note 7)		-	-	-	-	-
Other Assets (Note 8)	28	-	28	21	-	21
Total Intragovernmental Assets	$ 96,857	$ 1,386	$ 98,243	$ 99,839	$ 858	$ 100,697
Investments (Note 5)	201		201	$ 122		122
Accounts Receivable (net) (Note 7)	553	93	646	380	111	491
Loan Receivables and Related Foreclosed Property (net) (Note 9)	10,818	-	10,818	11,238	-	11,238
General Property Plant and Equipment (net) (Note10)	141	-	141	96	-	96
Other Assets (Note 8)	425	95	520	435	115	550
Total Assets	$ 108,995	$ 1,574	$ 110,569	$ 112,110	$ 1,084	$ 113,194

Note 7 – Accounts Receivable

The Department's accounts receivable represents Section 8 year-end settlements, claims to cash from the public and state and local authorities for bond refundings, sustained audit findings, FHA insurance premiums, and foreclosed property proceeds. A 100 percent allowance for loss is established for all delinquent accounts 90 days and over.

Section 8 Settlements

Section 8 subsidies disbursed during the year under annual contribution contracts are based on estimated amounts due under the contracts by PHAs. At the end of each year the actual amount due under the contracts is determined. The excess of subsidies paid to PHAs during the year over the actual amount due is reflected as accounts receivable in the balance sheet. These amounts are "collected" by offsetting such amounts with subsidies due to PHAs in subsequent periods. As of September 30, 2005 and 2004, the amounts totaled $220 million and $120 million, respectively.

Bond Refundings

Many of the Section 8 projects constructed in the late 1970s and early 1980s were financed with tax-exempt bonds with maturities ranging from 20 to 40 years. The related Section 8 contracts provided that the subsidies would be based on the difference between what tenants could pay pursuant to a formula, and the total operating costs of the Section 8 project, including debt service. The high interest rates during the construction period resulted in high subsidies. When interest rates came down in the 1980s, HUD was interested in getting the bonds refunded. One method used to account for the savings when bonds are refunded (PHAs sell a new series of bonds at a lower interest rate, to liquidate the original bonds) is to continue to pay the original amount of the bond debt service to a trustee. The amounts paid in excess of the lower "refunded" debt service and any related financing costs, are considered savings. One-half of these savings are provided to the PHA, the remaining half is returned to HUD. As of September 30, 2005 and 2004, HUD was due $90 million and $108 million, respectively.

Other Receivables

Other receivables include sustained audit findings, refunds of overpayment, FHA insurance premiums, and foreclosed property proceeds due from the public.

The following shows accounts receivable as reflected in the Balance Sheet as of September 30, 2005, and 2004, as follows (dollars in millions):

	FY 2005			FY 2004		
Description	Gross Accounts Receivable	Allowance for Loss	Total	Gross Accounts Receivable	Allowance for Loss	Total
Section 8 Settlements	$ 220	-	$ 220	$ 120	$ -	$ 120
Bond Refundings	101	$ (11)	90	119	(11)	108
Other Receivables:						
FHA Premiums	119	-	119	50	-	50
Other Receivables	300	(83)	217	296	(83)	213
Total	$ 740	$ (94)	$ 646	$ 585	$ (94)	$ 491

Note 8 – Other Assets

The following shows HUD's Other Assets as of September 30, 2005 (dollars in millions):

Description	FHA	Ginnie Mae	Section 8 Rental Assistance	All Other	Total
Intragovernmental Assets:					
Receivables from unapplied disbursements	-	-	-	-	-
Sec. 312 Rehabilitation Loan Program Receivables	-	-	-	-	-
Mortgagor Reserves for Replacement - Investment	-	-	-	-	-
Other Assets	-	-	-	$ 28	28
Total Intragovernmental Assets	-	-	-	28	28
Receivables Related to Asset Sales	-	-	-	-	-
Receivables Related to Credit Program Assets	-	-	-	-	-
Equity Interest in Multifamily Mortgage Trust 1996	-	-	-	-	-
GNMA Real Estate Owned Property and Hole Mortgages	-	-	-	-	-
Mortgagor Reserves for Replacement - Cash	$ 95	-	-	-	$ 95
Undeposited Collections	-	-	-	-	-
Advances to the Public	-	-	-	$ 1	1
Other Assets	2	$ 422	-	-	424
Total	$ 97	$ 422	-	$ 29	$ 548

The following shows HUD's Other Assets as of September 30, 2004 (dollars in millions):

Description	FHA	Ginnie Mae	Section 8 Rental Assistance	All Other	Total
Intragovernmental Assets:					
Receivables from unapplied disbursements	-	-	-	-	-
Sec. 312 Rehabilitation Loan Program Receivables	-	-	-	-	-
Mortgagor Reserves for Replacement - Investment	-	-	-	-	-
Other Assets	-	-	-	$ 21	21
Total Intragovernmental Assets	-	-	-	$ 21	$ 21
Receivables Related to Asset Sales	-	-	-	-	-
Receivables Related to Credit Program Assets	-	-	-	-	-
GNMA Real Estate Owned Property and Hole Mortgages	-	-	-	-	-
Equity Interest in Multifamily Mortgage Trust 1996	-	-	-	-	-
Premiums Receivable	-	-	-	-	-
Mortgagor Reserves for Replacement - Cash	$ 115	-	-	-	$ 115
Undeposited Collections	-	-	-	-	-
Advances from the Public	-	-	-	$ 2	2
Other Assets	5	$ 428	-	-	433
Total	$ 120	$ 428	$ -	$ 23	$ 571

Note 9 – Direct Loans and Loan Guarantees, Non-Federal Borrowers

HUD reports direct loan obligations or loan guarantee commitments made prior to FY 1992 and the resulting direct loans or defaulted guaranteed loans, net of allowance for estimated uncollectible loans or estimated losses.

Direct loan obligations or loan guarantee commitments made after FY 1991, and the resulting direct loans or defaulted guaranteed loans, are governed by the Federal Credit Reform Act of 1990, and are recorded as the net present value of the associated cash flows (i.e. interest rate differential, interest subsidies, estimated delinquencies and defaults, fee offsets, and other cash flows). The following is an analysis of loan receivables, loan guarantees, liability for loan guarantees, and the nature and amounts of the subsidy costs associated with the loans and loan guarantees for FY 2004 and 2003:

A. List of HUD's Direct Loan and/or Loan Guarantee Programs:

1. FHA
2. Housing for the Elderly and Disabled
3. Low Rent Public Housing Loan Fund
4. All Other
    a) Revolving Fund
    b) Flexible Subsidy
    c) CDBG Section 108(b)
    d) Indian Housing Loan Guarantee Fund
    e) Loan Guarantee Recovery Fund
    f) Native Hawaiian Housing Loan Guarantee Fund
    g) Title VI Indian Housing Loan Guarantee Fund

B. Direct Loans Obligated Prior to FY 1992 (Allowance for Loss Method)(dollars in millions):

2005

Direct Loan Programs	Loans Receivable, Gross	Interest Receivable	Allowance for Loan Losses	Foreclosed Property	Value of Assets Related to Direct Loans
FHA	$ 17	$ 3	$ (7)	-	$ 13
Housing for Elderly and Disabled	6,502	70	(19)	$ 7	6,560
Low Rent Public Housing Loans	1	-	-	-	1
All Other	694	6	(502)	2	200
Total	$ 7,214	$ 79	$ (528)	$ 9	$ 6,774

2004

Direct Loan Programs	Loans Receivable, Gross	Interest Receivable	Allowance for Loan Losses	Foreclosed Property	Value of Assets Related to Direct Loans
FHA	$ 22	$ 3	$ (12)	-	$ 13
Housing for Elderly and Disabled	6,991	78	(18)	$ 31	7,082
Low Rent Public Housing Loans	1	1	-	-	2
All Other	714	7	(516)	1	206
Total	$ 7,728	$ 89	$ (546)	$ 32	$ 7,303

C. Direct Loans Obligated After FY 1991(dollars in millions):

2005

Direct Loan Programs	Loans Receivable, Gross	Interest Receivable	Allowance for Subsidy Cost (Present Value)	Foreclosed Property	Value of Assets Related to Direct Loans
FHA	1	-	$ (3)	-	$ (2)

2004

Direct Loan Programs	Loans Receivable, Gross	Interest Receivable	Allowance for Subsidy Cost (Present Value)	Foreclosed Property	Value of Assets Related to Direct Loans
FHA	$ -	$ -	$ (3)	$ -	$ (3)

D. Defaulted Guaranteed Loans from Pre-1992 Guarantees (Allowance for Loss Method)(dollars in millions):

2005

	Defaulted Guaranteed Loans Receivable, Gross	Interest Receivable	Allowance for Loan and Interest Losses	Foreclosed Property, Net	Defaulted Guaranteed Loans Receivable, Net
FHA	$ 2,973	$ 140	$ (847)	$ 25	$ 2,291

2004

	Defaulted Guaranteed Loans Receivable, Gross	Interest Receivable	Allowance for Loan and Interest Losses	Foreclosed Property, Net	Defaulted Guaranteed Loans Receivable, Net
FHA	$ 2,760	$ 135	$ (905)	$ 15	$ 2,005

E. Defaulted Guaranteed Loans From Post-FY 1991 Guarantees (dollars in millions):

2005

	Defaulted Guaranteed Loans Receivable, Gross	Interest Receivable	Allowance for Subsidy Cost (Present Value)	Foreclosed Property, Gross	Value of Assets Related to Defaulted Guaranteed Loans
FHA	$ 998	$ 61	$ (2,096)	$ 2,792	$ 1,755

2004

	Defaulted Guaranteed Loans Receivable, Gross	Interest Receivable	Allowance for Subsidy Cost (Present Value)	Foreclosed Property, Gross	Value of Assets Related to Defaulted Guaranteed Loans
FHA	$ 1,044	$ 74	$ (1,675)	$ 2,490	$ 1,933

	2005	2004
Total Credit Program Receivables and Related Foreclosed Property, Net	**$10,818**	**11,238**

F. Guaranteed Loans Outstanding (dollars in millions):

Guaranteed Loans Outstanding:

Loan Guarantee Programs	2005 Outstanding Principal, Guaranteed Loans, Face Value	2005 Amount of Outstanding Principal Guaranteed
FHA Programs	$ 454,372	$ 416,461
All Other	2,621	2,621
Total	$ 456,993	$ 419,082

Loan Guarantee Programs	2004 Outstanding Principal, Guaranteed Loans, Face Value	2004 Amount of Outstanding Principal Guaranteed
FHA Programs	$ 507,115	$ 468,796
All Other	2,548	2,548
Total	$ 509,663	$ 471,344

New Guaranteed Loans Disbursed (Current Reporting Year)

Loan Guarantee Programs	Outstanding Principal, Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
FHA Programs	$ 66,290	$ 65,773
All Other	251	251
Total	$ 66,541	$ 66,024

New Guaranteed Loans Disbursed (Prior Reporting Years)

Loan Guarantee Programs	Outstanding Principal, Guaranteed Loans, Face Value	Amount of Outstanding Principal Guaranteed
FHA Programs	$ 117,381	$ 116,139
All Other	403	403
Total	$ 117,784	$ 116,542

G. Liability for Loan Guarantees (Estimated Future Default Claims, Pre-1992)(dollars in millions):

	2005		
Loan Guarantee Programs	Liabilities for Losses on Pre-1992 Guarantees, Estimated Future Default Claims	Liabilities for Loan Guarantees for Post-1991 Guarantees (Present Value)	Total Liabilities For Loan Guarantees
FHA Programs	$ 1,217	$ 3,367	$ 4,584
All Other	-	94	94
Total	$ 1,217	$ 3,461	$ 4,678

	2004		
Loan Guarantee Programs	Liabilities for Losses on Pre-1992 Guarantees, Estimated Future Default Claims	Liabilities for Loan Guarantees for Post-1991 Guarantees (Present Value)	Total Liabilities For Loan Guarantees
FHA Programs	$ 2,349	$ 2,725	$ 5,074
All Other	-	97	97
Total	$ 2,349	$ 2,822	$ 5,171

H. Subsidy Expense for Post-FY 1991 Loan Guarantees:

Subsidy Expense for Current Year Loan Guarantees (dollars in millions)

	2005			
Loan Guarantee Programs	Default Component	Fees Component	Other Component	Subsidy Amount
FHA	$ 1,910	$ (3,406)	$ 271	$ (1,225)
All Other	6	-	-	6
Total	$ 1,916	$ (3,406)	$ 271	$ (1,219)

	2004			
Loan Guarantee Programs	Default Component	Fees Component	Other Component	Subsidy Amount
FHA	$ 2,252	$ (5,578)	$ 388	$ (2,938)
All Other	10	-	-	10
Total	$ 2,262	$ (5,578)	$ 388	$ (2,928)

Modification and Re-estimates (dollars in millions)

Loan Guarantee Programs	2005 Total Modifications	2005 Interest Rate Re-estimates	2005 Technical Re-estimates	2005 Total Re-estimates
FHA	(78)	-	$ 1,921	$ 1,843
All Other			6	6
Total	$ (78)	$ -	$ 1,927	$ 1,849

Loan Guarantee Programs	2004 Total Modifications	2004 Interest Rate Re-estimates	2004 Technical Re-estimates	2004 Total Re-estimates
FHA	-	-	$ 2,494	$ 2,494
All Other			$ 26	$ 26
Total	$ -	$ -	$ 2,520	$ 2,520

Total Loan Guarantee Subsidy Expense (dollars in millions)

Loan Guarantee Programs	Current Year	Prior Year
FHA	$ 618	$ (444)
All Other	-	36
Total	$ 618	$ (408)

I. Subsidy Rates for Loan Guarantees by Programs and Component:

Budget Subsidy Rates for Loans Guarantee for FY 2005

Loan Guarantee Program	Interest Rate Differential	Default	Fees and Other Collections	Other	Total
FHA					
FHA	0.00%	2.05%	-4.30%	0.46%	-1.79%
FHA- Other	0.00%	3.51%	-4.41%		-0.90%
All Other					
CDBG, Section 108 (b)	0.00%	2.30%			2.30%
Loan Guarantee Recovery	0.00%	50.00%			50.00%
Indian Housing	0.00%	2.58%			2.58%
Native Hawaiian Housing	0.00%	2.58%			2.58%
Title VI Indian Housing	0.00%	10.32%			10.32%

The subsidy rates above pertain only to FY 2005 cohorts. These rates cannot be applied to the guarantees of loans disbursed during the current reporting year to yield the subsidy expense. The subsidy expense for new loan guarantees reported in the current year could result from disbursements of loans from both current year cohorts and prior year(s) cohort. The subsidy expense reported in the current year also includes modifications and re-estimates.

J. Schedule for Reconciling Loan Guarantee Liability Balances (post-1991 Loan Guarantees):
(dollars in millions)

Beginning Balance, Changes, and Ending Balance	FY 2005	FY 2004
Beginning balance of the loan guarantee liability	$ 5,172	$ 6,313
Add: subsidy expense for guaranteed loans disbursed during the reporting years by component:		
(a) Interest supplement costs	-	-
(b) Default costs (net of recoveries)	1,916	2,289
(c) Fees and other collections	(3,406)	(5,577)
(d) Othe subsidy costs	271	387
Total of the above subsidy expense components	$ (1,219)	$ (2,901)
Adjustments:		
(a) Loan guarantee modifications	-	-
(b) Fees Received	2,482	2,914
(c) Interest supplemental paid	-	-
(d) Foreclosed property and loans acquired	5,753	6,367
(e) Claim payments to lenders	(8,506)	(9,116)
(f) Interest accumulation on the liability balance	(51)	(223)
(g) Other	42	44
Ending balance of the subsidy cost allowance before re-estimates	$ 3,673	$ 3,398
Add or Subtract subsidy re-estimates by component:		
(a) Interest rate re-estimate	198	-
(b) Technical/default re-estimate	807	1,774
Total of the above re-estimate components	1,005	1,774
Ending balance of the subsidy cost allowance	$ 4,678	$ 5,172

K. Administrative Expense (dollars in millions):

Loan Guarantee Program	FY 2005	FY 2004
FHA	$ 473	$ 425
All Other	1	1
Total	$ 474	$ 426

Note 10 – General Property, Plant, and Equipment

General property, plant, and equipment consists of furniture, fixtures, equipment, and data processing software used in providing goods and services that have an estimated useful life of two or more years. Purchases of $100,000 or more are recorded as an asset and depreciated over their estimated useful life on a straightline basis with no salvage value. Capitalized replacement and improvement costs are depreciated over the remaining useful life of the replaced or improved asset. Generally, the Department's assets are depreciated over a four-year period, unless it can be demonstrated that the estimated useful life is significantly greater than four years.

The following shows general property, plant, and equipment as of September 30, 2005 and 2004 (dollars in millions).

Description	FY 2005			FY 2004		
	Cost	Accum Depr and Amortization	Book Value	Cost	Accum Depr and Amortization	Book Value
Equipment	$ 31	$ (27)	$ 4	$ 31	$ (27)	$ 4
Leasehold Improvements	5	(2)	3	4	(2)	2
Internal Use Software	92	(46)	46	76	(39)	37
Internal Use Software in Development	88	-	88	53	-	53
Total Assets	$ 216	$ (75)	$ 141	$ 164	$ (68)	$ 96

Note 11 – Liabilities Covered and Not Covered by Budgetary Resources

The following shows HUD’s liabilities as of September 30, 2005, and 2004 (dollars in millions):

Description	2005			2004		
	Covered	Not-Covered	Total	Covered	Not-Covered	Total
Intragovernmental						
Accounts Payable	$ -	-	$ -	$ -	-	$ -
Debt	8,922	$ -	8,922	10,102	$ -	10,102
Other Intragovernmental Liabilities	977	18	995	772	18	790
Total Intragovernmental Liabilities	$ 9,899	$ 18	$ 9,917	$ 10,874	$ 18	$ 10,892
Accounts Payable	847	-	847	817	-	817
Liabilities for Loan Guarantees	4,678	-	4,678	5,172	-	5,172
Debt	1,542	-	1,542	1,858	-	1,858
Federal Employee and Veterans' Benefits	-	82	82	-	79	79
Loss Reserves	539	-	539	519	-	519
Other Liabilities	941	73	1,014	1,128	71	1,199
Total Liabilities	$ 18,446	$ 173	$ 18,619	$ 20,368	$ 168	$ 20,536

Note 12 – Debt

Several HUD programs have the authority to borrow funds from the U.S. Treasury for program operations. Additionally, the National Housing Act authorizes FHA, in certain cases, to issue debentures in lieu of cash to pay claims. Also, PHAs and Tribally Designated Housing Entities borrowed funds from the private sector and from the Federal Financing Bank to finance construction and rehabilitation of low rent housing. HUD is repaying these borrowings on behalf of the PHAs and the Tribally Designated Housing Entities.

The following shows HUD borrowings, and borrowings by PHAs/Tribally Designated Housing Entities for which HUD is responsible for repayment, as of September 30, 2005 (dollars in millions):

Description	Beginning Balance	Net Borrowings	Ending Balance
Agency Debt:			
Held by Government Accounts	$ 1,183	$ (93)	$ 1,090
Held by the Public	1,858	(316)	1,542
Total Agency Debt	$ 3,041	$ (409)	$ 2,632
Other Debt:			
Debt to the U.S. Treasury	$ 8,919	$ (1,087)	$ 7,832
Total Debt	$ 11,960	$ (1,496)	$ 10,464
Classification of Debt:			
Intragovernmental Debt			$ 8,922
Debt held by the Public			1,542
Debentures Issued to Claimants			-
Total Debt			$ 10,464

The following shows HUD borrowings, and borrowings by PHAs/Tribally Designated Housing Entities for which HUD is responsible for repayment, as of September 30, 2004 (dollars in millions):

Description	Beginning Balance	Net Borrowings	Ending Balance
Agency Debt:			
Held by Government Accounts	$ 1,270	$ (87)	$ 1,183
Held by the Public	2,210	(352)	1,858
Total Agency Debt	$ 3,480	$ (439)	$ 3,041
Other Debt:			
Debt to the U.S. Treasury	$ 11,542	$ (2,623)	$ 8,919
Debt to the Federal Financing Bank	2	(2)	-
Total Other Debt	$ 11,544	$ (2,625)	$ 8,919
Total Debt	$ 15,024	$ (3,064)	$ 11,960
Classification of Debt:			
Intragovernmental Debt			$ 10,102
Debt held by the Public			1,858
Debentures Issued to Claimants			-
Total Debt			$ 11,960

Interest paid on borrowings during the year ended September 30, 2005, and 2004, was $1 billion and $1.1 billion, respectively. The purpose of these borrowings is discussed in the following paragraphs.

Borrowings from the U.S. Treasury

HUD is authorized to borrow from the U.S. Treasury to finance Housing for Elderly and Disabled loans. The Treasury borrowings typically have a 15-year term, but may be repaid prior to maturity at HUD's discretion. However, such borrowings must be repaid in the sequence in which they were borrowed from Treasury. The interest rates on the borrowings are based on Treasury's 30-year bond yield at the time the notes are issued. Interest is payable on April 30 and October 31. Interest rates ranged from 7.44 percent to 8.18 percent during FY 2005 and 7.44 percent to 8.80 percent for FY 2004.

In FY 2005 and 2004, FHA borrowed $1.2 billion and $3.4 billion respectively from the U.S. Treasury. The borrowings were needed when FHA initially determined negative credit subsidy amounts related to new loan disbursements or to existing loan modifications. In some instances, borrowings were needed where available cash was less than claim payments due or downward subsidy-estimates. All borrowings were made by FHA's financing accounts. Negative subsidies were generated primarily by the Mutual Mortgage Insurance/Cooperative Management Housing Insurance Fund financing account; downward re-estimates have occurred from activity of the FHA's loan guarantee financing accounts. These borrowings carried interest rates ranging from 2.41 percent to 7.34 percent during FY 2005 and from 3.71 percent to 7.34 percent during FY 2004.

Borrowings from the Federal Financing Bank and the Public

During the 1960s, 1970s, and 1980s, PHAs obtained loans from the private sector and from the Federal Financing Bank to finance development and rehabilitation of low rent housing projects. HUD is repaying these borrowings on behalf of the PHAs, through the Low Rent Public Housing program. For borrowings from the public, interest is payable throughout the year. Interest rates ranged from 3.25 percent to 6.0 percent during FY 2005, and from 3.25 percent to 6.0 percent during FY 2004. The borrowings from the Federal Financing Bank and the private sector have terms up to 40 years. Federal Financing Bank interest is payable annually on November 1. Interest rates ranged from 10.67 percent to 16.18 percent during both FY 2005 and 2004.

Before July 1, 1986, the Federal Financing Bank purchased notes issued by units of general local government and guaranteed by HUD under Section 108. These notes had various maturities and carried interest rates that were one-eighth of one percent above rates on comparable Treasury obligations. The Federal Financing Bank still holds substantially all outstanding notes, and no note purchased by the Bank has ever been declared in default.

Debentures Issued To Claimants

The National Housing Act authorizes FHA, in certain cases, to issue debentures in lieu of cash to settle claims. FHA-issued debentures bear interest at rates established by the U.S. Treasury. Interest rates related to the outstanding debentures ranged from 4.00 percent to 12.88 percent during both FY 2005 and FY 2004. Debentures may be redeemed by lenders prior to maturity to pay mortgage insurance premiums to FHA, or they may be called with the approval of the Secretary of the U.S. Treasury.

Note 13 – Other Liabilities

The following shows HUD's Other Liabilities as of September 30, 2005 (dollars in millions):

Description	Non-Current	Current	Total
Intragovernmental Liabilities			
FHA Payable from Unapplied Receipts Recorded by Treasury	-	-	-
Special Receipt Account Liability	-	$ 771	$ 771
HUD-Section 312 Rehabilitation Program Payable	-	-	-
Unfunded Federal Employees' Compensation Act Liability	$ 18	-	18
Resource Payable to Treasury	-	-	-
Miscellaneous Receipts Payable to Treasury	121	-	121
Other Liabilities	-	85	85
Total Intragovernmental Liabilities	$ 139	$ 856	$ 995
Other Liabilities			
FHA Other Liabilities	$ -	$ 226	$ 226
FHA Escrow Funds Related to Mortgage Notes	-	170	170
FHA Unearned Premiums	(50)	27	(23)
Ginnie Mae Deferred Income	-	77	77
Deferred Credits	-	1	1
Deposit Funds	67	2	69
Accrued Unfunded Annual Leave	72	-	72
Accrued Funded Payroll Benefits	36	-	36
Other		386	386
Total Other Liabilities	$ 264	$ 1,745	$ 2,009

Special Receipt Account Liability

The special receipt account liability is created from negative subsidy endorsements and downward credit subsidies in the General Insurance/Special Risk Insurance special receipt account.

The following shows HUD's Other Liabilities as of September 30, 2004 (dollars in millions):

Description	Non-Current	Current	Total
Intragovernmental Liabilities			
FHA Payable from Unapplied Receipts			
Recorded by Treasury	-	-	-
Special Receipt Account Liability	-	$ 627	$ 627
HUD-Section 312 Rehabilitation Program Payable	-	-	-
Unfunded Federal Employees' Compensation Act Liability	-	18	18
Resource Payable to Treasury	$ -	-	-
Miscellaneous Receipts Payable to Treasury	141	-	141
Other Liabilities	-	4	4
Total Intragovernmental Liabilities	$ 141	$ 649	$ 790
Other Liabilities			
FHA Other Liabilities	$ -	$ 229	$ 229
FHA Escrow Funds Related to Mortgage Notes	-	189	189
FHA Unearned Premiums	137	35	172
Ginnie Mae Deferred Income	-	75	75
Deferred Credits	-	-	-
Deposit Funds	12	28	40
Accrued Unfunded Annual Leave	71	-	71
Accrued Funded Payroll Benefits	37	-	37
Other	-	386	386
Total Other Liabilities	$ 398	$ 1,591	$ 1,989

Note 14 – Loss Reserves

For FY 2005 and 2004, Ginnie Mae established loss reserves of $539 million and $519 million, respectively, which represents probable defaults by issuers of mortgage-backed securities, through a provision charged to operations. The reserve is relieved as losses are realized from the disposal of the defaulted issuers' portfolios. Ginnie Mae recovers part of its losses through servicing fees on the performing portion of the portfolios and the sale of servicing rights, which transfers to Ginnie Mae upon the default of the issuer. Ginnie Mae management believes that its reserve is adequate to cover probable losses from defaults by issuers of Ginnie Mae guaranteed mortgage-backed securities.

Ginnie Mae incurs losses when insurance and guarantees do not cover expenses that result from issuer defaults. Such expenses include: (1) unrecoverable losses on individual mortgage defaults because of coverage limitations on mortgage insurance or guarantees, (2) ineligible mortgages included in defaulted Ginnie Mae pools, (3) improper use of proceeds by an issuer, and, (4) non-reimbursable administrative expenses and costs incurred to service and liquidate portfolios of defaulted issuers.

Note 15 – Financial Instruments with Off-Balance Sheet Risk

Some of HUD's programs, principally those operated through FHA and Ginnie Mae, enter into financial arrangements with off-balance sheet risk in the normal course of their operations.

A. FHA Mortgage Insurance

Unamortized insurance in force outstanding for FHA's mortgage insurance programs as of September 30, 2005 and 2004, was $454 billion and $507 billion, respectively, and is discussed in Note 9F.

B. Ginnie Mae Mortgage-Backed Securities

Ginnie Mae financial instruments with off-balance sheet risk include guarantees of mortgage-backed securities and commitments to guaranty those securities. The securities are backed by pools of FHA-insured, Rural Housing Service-insured, and Veterans Affairs-guaranteed mortgage loans. Ginnie Mae is exposed to credit loss in the event of non-performance by other parties to the financial instruments. The total amount of Ginnie Mae guaranteed securities outstanding at September 30, 2005 and 2004, was approximately $412.3 billion and $453.4 billion, respectively. However, Ginnie Mae's potential loss is considerably less because the FHA and Rural Housing Service insurance and Department of Veterans Affairs guaranty serve to indemnify Ginnie Mae for most losses. Also, as a result of the structure of the security, Ginnie Mae bears no interest rate or liquidity risk.

During the mortgage closing period and prior to granting its guaranty, Ginnie Mae enters into commitments to guaranty mortgage-backed securities. The commitment ends when the securities are issued or when the commitment period expires. Ginnie Mae's risks related to outstanding commitments are much less than for outstanding securities due, in part, to Ginnie Mae's ability to limit commitment authority granted to individual issuers of mortgage-backed securities. Outstanding commitments as of September 30, 2005 and 2004, were $55.1 billion and $42.9 billion, respectively. Generally, Ginnie Mae's securities pools are diversified among issuers and geographic areas. No significant geographic concentrations of credit risk exist; however, to a limited extent, securities are concentrated among issuers.

In FY 2005 and 2004, Ginnie Mae issued a total of $56.6 billion and $81.4 billion, respectively, in its multi-class securities program. The estimated outstanding balances at September 30, 2005 and 2004, were $185.9 billion and $189.1 billion, respectively. These guaranteed securities do not subject Ginnie Mae to additional credit risk beyond that assumed under the mortgage-backed securities program.

C. Section 108 Loan Guarantees

Under HUD's Section 108 Loan Guarantee program, recipients of CDBG Entitlement Grant program funds may pledge future grant funds as collateral for loans guaranteed by HUD (these loans were provided from private lenders since July 1, 1986). This Loan Guarantee Program provides entitlement communities with a source of financing for projects that are too large to be financed from annual grants. The amount of loan guarantees outstanding as of September 30, 2005 and 2004, was $2.3 billion. HUD's management believes its exposure in providing these loan guarantees is limited, since loan repayments can be offset from future CDBG Entitlement Program Funds and, if necessary, other funds provided to the recipient by HUD. HUD has never had a loss under this program since its inception in 1974.

Note 16 – Contingencies

The Department is subject to various claims and contingencies related to lawsuits incidental to its operations either brought by it or against it. For FY 2005, the Department was party to a number of suits with total claimed amounts of approximately $1.76 billion, plus other suits with unspecified claims. Of this claimed amount, $1.7 billion is linked to cases where the possibility of actual loss is considered remote. The Department had two cases where judgments were issued on September 30, with probable losses totaling $42 million, pending a decision to appeal on one and the results of an appeal on the other.

The Department acknowledges that there are other suits with probable, reasonable, and remote possibility of losses where the potential liabilities cannot be estimated. In the opinion of management, the ultimate resolution of pending litigation does not have a material effect on the Department's FY 2005 financial statements.

Note 17 – Rental Housing Subsidy Payment Errors

Note 17 is no longer required, as the issue has been downgraded from a material weakness to a reportable condition.

Note 18 – Total Cost and Earned Revenue by Budget Functional Classification

The following shows HUD's total cost and earned revenue by budget functional classification for FY 2005 (dollars in millions):

Budget Functional Classification	Gross Cost	Earned Revenue	Net Cost
Intragovernmental:			
Commerce and Housing Credit	$ 637	$ (1,948)	$ (1,311)
Community and Regional			
Development	19	(5)	14
Income Security	491	(4)	487
Administration of Justice	-	-	-
Miscellaneous	-	-	-
Total Intragovernmental	$ 1,147	$ (1,957)	$ (810)
With the Public:			
Commerce and Housing Credit	$ 708	$ (1,252)	$ (544)
Community and Regional			
Development	5,485	-	5,485
Income Security	36,244	(17)	36,227
Administration of Justice	47	-	47
Miscellaneous	-	-	-
Total with the Public	$ 42,484	$ (1,269)	$ 41,215
TOTAL:			
Commerce and Housing Credit	$ 1,345	$ (3,200)	$ (1,855)
Community and Regional	-	-	-
Development	5,504	(5)	5,499
Income Security	36,735	(21)	36,714
Administration of Justice	47	-	47
Miscellaneous	-	-	-
TOTAL:	$ 43,631	$ (3,226)	$ 40,405

The following shows HUD's total cost and earned revenue by budget functional classification for FY 2004 (dollars in millions):

Budget Functional Classification	Gross Cost	Earned Revenue	Net Cost
Intragovernmental:			
Commerce and Housing Credit	$ 892	$ (1,994)	$ (1,102)
Community and Regional Development	44	(4)	40
Income Security	448	(1)	447
Administration of Justice	-	-	-
Miscellaneous	-	-	-
Total Intragovernmental	$ 1,384	$ (1,999)	$ (615)
With the Public:			
Commerce and Housing Credit	$ (533)	$ (1,248)	$ (1,781)
Community and Regional Development	5,842	(7)	5,835
Income Security	35,571	(16)	35,555
Administration of Justice	46	-	46
Miscellaneous	-	-	-
Total with the Public	$ 40,926	$ (1,271)	$ 39,655
TOTAL:			
Commerce and Housing Credit	$ 359	$ (3,242)	$ (2,883)
Community and Regional Development	5,886	(11)	5,875
Income Security	36,019	(17)	36,002
Administration of Justice	46	-	46
Miscellaneous	-	-	-
TOTAL:	$ 42,310	$ (3,270)	$ 39,040

Note 19 – Net Costs of HUD's Cross-Cutting Programs

This footnote provides a categorization of net costs for two of HUD's major program areas whose costs were incurred across multiple programs. Section 8 costs are incurred to assist low- and very low-income families in obtaining decent and safe rental housing. In addition, costs incurred under the other major program represent HUD's smaller programs. These programs provide assistance to support other HUD objectives such as fair housing and equal opportunity, energy conversation, homeless assistance, housing units rehabilitation, and home ownership.

The following shows HUD's major programs that incur costs across multiple program offices as of September 30, 2005 (dollars in millions):

HUD's Cross-Cutting Programs	Public and Indian Housing	Housing	Community Planning and Development	Other	Consolidated
Section 8:					
Intragovernmental Gross Costs	$ 37	$ 28	$ -	$ -	$ 65
Intragovernmental Earned Revenues	-	-	-	-	$ -
Intragovernmental Net Costs	$ 37	$ 28	$ -	$ -	$ 65
Gross Costs with the Public	$ 15,361	$ 7,948	$ 21	$ -	$ 23,330
Earned Revenues	-	-	-	-	$ -
Net Costs with the Public	$ 15,361	$ 7,948	$ 21	$ -	$ 23,330
Net Program Costs	$ 15,398	$ 7,976	$ 21	$ -	$ 23,395
Other:					
Intragovernmental Gross Costs	$ 31	$ 24	$ 43	$ 106	$ 204
Intragovernmental Earned Revenues	(1)	(1)	(4)	(3)	$ (9)
Intragovernmental Net Costs	$ 30	$ 23	$ 39	$ 103	$ 195
Gross Costs with the Public	$ 733	$ 632	$ 1,689	$ 794	$ 3,848
Earned Revenues	-	(24)	-	-	$ (24)
Net Costs with the Public	$ 733	$ 608	$ 1,689	$ 794	$ 3,824
Net Program Costs	$ 763	$ 631	$ 1,728	$ 897	$ 4,019

The following shows the cross-cutting of HUD's major program areas that incur costs across multiple program areas as of September 30, 2004 (dollars in millions):

HUD's Cross-Cutting Programs	Public and Indian Housing	Housing	Community Planning and Development	Other	Consolidated
Section 8:					
Intragovernmental Gross Costs	$ 39	$ 25	$ -	$ -	$ 64
Intragovernmental Earned Revenues	-	-	-	-	$ -
Intragovernmental Net Costs	$ 39	$ 25	$ -	$ -	$ 64
Gross Costs with the Public	$ 14,673	$ 7,715	$ 13	$ -	$ 22,401
Earned Revenues	-	-	-	-	$ -
Net Costs with the Public	$ 14,673	$ 7,715	$ 13	$ -	$ 22,401
Net Program Costs	$ 14,712	$ 7,740	$ 13	$ -	$ 22,465
Other:					
Intragovernmental Gross Costs	$ 33	$ 28	$ 37	$ 65	$ 163
Intragovernmental Earned Revenues	(1)	-	(4)	-	$ (5)
Intragovernmental Net Costs	$ 32	$ 28	$ 33	$ 65	$ 158
Gross Costs with the Public	$ 666	$ 651	$ 1,640	$ 459	$ 3,416
Earned Revenues	-	(25)	(7)	-	$ (32)
Net Costs with the Public	$ 666	$ 626	$ 1,633	$ 459	$ 3,384
Net Program Costs	$ 698	$ 654	$ 1,666	$ 524	$ 3,542

Note 20 – FHA Net Costs

FHA organizes its operations into two overall program types – Mutual Mortgage Insurance/Cooperative Management Housing Insurance and General Insurance/Special Risk Insurance. These program types are composed of four major funds. The Mutual Mortgage Insurance fund, FHA's largest fund, provides basic single family mortgage insurance and is a mutual insurance fund, whereby mortgagors, upon non-claim termination of their mortgages, share surplus premiums paid into the Mutual Mortgage Insurance fund that are not required for operating expenses and losses or to build equity. The Cooperative Management Housing Insurance fund, another mutual fund, provides mortgage insurance for management-type cooperatives. The General Insurance fund provides a large number of specialized mortgage insurance activities, including insurance of loans for property improvements, cooperatives, condominiums, housing for the elderly, land development, group practice medical facilities, and nonprofit hospitals. The Special Risk Insurance fund provides mortgage insurance on behalf of mortgagors eligible for interest reduction payments who otherwise would not be eligible for mortgage insurance.

The following table shows Net Cost detail for FHA as of September 30, 2005 and 2004 (dollars in millions):

	2005			2,004		
	GI/SRI Program	MMI/CMHI Program	Total	GI/SRI Program	MMI/CMHI Program	Total
Costs						
Intragovernmental Gross Costs	$ 127	$ 405	$ 532	$ 88	$ 631	$ 719
Intragovernmental Earned Revenues	(147)	(1,344)	(1,491)	(92)	(1,460)	(1,552)
Intragovernmental Net Costs	$ (20)	$ (939)	$ (959)	$ (4)	$ (829)	$ (833)
Gross Costs with the Public	$ (989)	$ 1,243	$ 254	$ (231)	$ (436)	$ (667)
Earned Revenues	(322)	(41)	(363)	(186)	(64)	(250)
Net Costs with the Public	$ (1,311)	$ 1,202	$ (109)	$ (417)	$ (500)	$ (917)
Net Program Costs	$ (1,331)	$ 263	$ (1,068)	$ (421)	$ (1,329)	$ (1,750)

Note 21 – Prior Period Adjustments

There were no prior period adjustments.

Note 22 – Apportionment Categories of Obligations Incurred

Budgetary resources are usually distributed in an account or fund by specific time periods, activities, projects, objects, or a combination of these categories. Resources apportioned by fiscal quarters are classified as Category A apportionments. Apportionments by any other category would be classified as Category B apportionments. HUD's categories of obligations incurred were as follows (dollars in millions):

Fiscal Year	Category A	Category B	Exempt From Apportionment	Total
2005	$ 1,263	$ 53,264	$ -	$ 54,527
2004	$ 1,250	$ 60,841	$ -	$ 62,091

Note 23 – Explanation of Differences Between the Statement of Budgetary Resources and the Budget of the United States Government

The President's Budget containing actual FY 2005 data is not available for comparison to the Statement of Budgetary Resources.

For FY 2004, an extensive analysis to compare HUD's Statement of Budgetary Resources to the President's Budget of the United States was performed to identify any differences. The Department's Statement of Budgetary Resources includes unobligated balances totaling $470 million as of September 30, 2004, which are not reported in the President's Budget of the United States. OMB's Circular No. A-11: Preparation, Submission, and Execution of the Budget, requires that any unobligated balances reported in the President's Budget exclude any amounts from funds expiring at the end of the current fiscal year. These programs, reported in the Department's financial statements, consist of administrative accounts appropriated on an annual basis and other grant programs that receive both multi-year and no-year funding authorizations from Congress.

The following shows the difference between Unobligated Balance Carried Forward reported in the Statement of Budgetary Resources and the President's Budget as of September 30, 2004 (dollars in millions):

Unobligated Balance Carried Forward, End of Year	Statement of Budgetary Resources		United States Budget	Differences	Explanation Note
FHA	$28,172		$27,912	$260	1
Ginnie Mae	10,841		10,571	270	2
Section 8 Rental Assistance	2,254		2,253	1	3
CDBG	1,346		1,305	41	1
HOME	457	#	448	9	1
Operating Subsidy	3		3	-	
PIH Loans and Grants	398		398	-	
Housing for the Elderly & Disabled	1,664		1,622	42	1
All Other	3,905		3,785	120	4
Total	$49,040		$48,297	$743	

Explanation Notes:

1 - Activity in expired accounts is reflected in the Statement of Budgetary Resources; however, it is not included in the President's Budget.

2 - The President's Budget reported $260 million in defaulted portfolios seized by Ginnie Mae in FY 2004 as defaulted claim payments. This $260 million represents the remaining principal balance of the securities in the portfolio and is NOT a liability or a potential liability. Ginnie Mae takes possession of mortgage-backed securities portfolios at the time of issuer default; however, Ginnie Mae DOES NOT purchase these portfolios when taking possession. Consequently, NO CASH OUTLAYS are made when Ginnie Mae acquires a mortgage-backed securities portfolio. At the time of default, Ginnie Mae takes possession of the security portfolio servicing assets (which have value) and any corresponding liabilities. The incorrect reporting of $260 million in defaults in turn incorrectly reported total obligations and unobligated balance carried forward in FY 2004. Therefore, total new obligations for FY 2004 should be $429 million and not $689 million as reported in the President's Budget. The $10 million additional difference is in the Receipt Account and is due to the change in requirements for posting negative subsidy transfer to the Receipt Account.

3 - Rounding

4 - $113 million is activity in expired accounts that is not reflected in the President's Budget, $3 million is due to rounding on different programs and $4 million for the Appalachian Regional Commission program is reported in the Other Independent Agency section of the President's Budget.

The following shows the difference between Outlays reported in the Statement of Budgetary Resources and the President's Budget as of September 30, 2004 (dollars in millions):

Outlays reported	Statement of Budgetary Resources	United States Budget	Differences	Explanation Note
FHA	$292	$293	($1)	1
Ginnie Mae	(350)	(350)	-	
Section 8 Rental Assistance	22,362	22,356	6	2
CDBG	5,400	5,388	12	2
HOME	1,607	1,597	10	2
Operating Subsidy	3,434	3,434	-	2
PIH Loans and Grants	4,147	4,088	59	2
Housing for the Elderly & Disabled	244	244	-	
All Other	3,827	3,879	(52)	3
Total	$40,963	$40,929	$34	

Explanation Notes:

1 - Rounding

2 - Represents HUD's Intragovernmental activity not eliminated in the Department's FY 2004 audited financial statements. The Department's methodology for eliminating intragovernmental receipts and collections was revised in FY 2005 to ensure consistency between the amounts of outlays reported in the President's Budget and the audited financial statements.

3 - $58 million is representative in the intragovermental activity explained above. $6 million is for the Appalachian Regional Commission program reported in the Other Independent Agencies section of the President's Budget.

The following shows the difference between Offsetting Receipts reported in the Statement of Budgetary Resources and the President's Budget as of September 30, 2004 (dollars in millions):

Offsetting Receipts	Statement of Budgetary Resources	United States Budget	Differences	Explanation Note
FHA	$419	$419	-	
Ginnie Mae	-	-	-	
All Other	16	16	-	
Total	$435	$435	-	

The following shows the difference between Unpaid Obligations reported in the Statement of Budgetary Resources and the President's Budget as of September 30, 2004 (dollars in millions):

Unpaid Obligations	Statement of Budgetary Resources	United States Budget	Differences	Explanation Note
FHA	$ 1,868	$ 1,868	$ -	
Ginnie Mae	36	296	(260)	1
Section 8 Rental Assistance	26,383	26,383	-	
CDBG	10,693	10,694	(1)	2
HOME	5,247	5,247	-	
Operating Subsidy	2,007	2,007	-	
PIH Loans and Grants	11,140	11,140	-	
Housing for the Elderly & Disabled	5,496	5,496	-	
All Other	13,435	13,426	9	3
Total	$76,305	$76,557	($252)	

Explanation Notes:

1 - The President's Budget reported $260 million in defaulted portfolios seized by Ginnie Mae in FY 2004 as defaulted claim payments. This $260 million represents the remaining principal balance of the securities in the portfolio and is NOT a liability or a potential liability. Ginnie Mae takes possession of mortgage-backed securities portfolios at the time of issuer default; however, Ginnie Mae DOES NOT purchase these portfolios when taking possession. Consequently, NO CASH OUTLAYS are made when Ginnie Mae acquires a mortgage-backed securities portfolio. At the time of default Ginnie Mae takes possession of the security portfolio servicing assets (which have value) and any corresponding liabilities. The incorrect reporting of $260 million in defaults in turn incorrectly reported total obligations and unobligated balance carried forward in FY 2004. Therefore, total new obligations for FY 2004 should be $429 million and not $689 million as reported in the President's Budget.

2 - Rounding

3 - $3 million due to rounding and $12 million is for the Appalachian Regional Commission program reported in the Other Independent Agencies section of the President's Budget.

Note 24 – Explanation of the Relationship Between Liabilities Not Covered by Budgetary Resources on the Balance Sheet and the Changes in Components Requiring or Generating Resources in Future Periods

In FY 2005, the Department reported a net increase in unfunded annual leave liability in the amount of $2 million in the Consolidated Statement of Financing. This unfunded leave liability is not covered by budgetary resources at the balance sheet date.

Consolidating Balance Sheet
As of September 2005
(Dollars in millions)

	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
ASSETS				
Intragovernmental				
Fund Balance with Treasury (Note 3)	$9,705	$3,711	$10,701	$11,877
Investments (Note 5)	22,744	7,971		
Accounts Receivable (Note 7)				
Other Assets (Note 8)	53		6	10
Total Intragovernmental Assets (Note 6)	$32,503	$11,682	$10,708	$11,887
Investments (Net) (Note 5)	201			
Accounts Receivable (Net) (Note 7)	302	28	310	
Credit Program Receivables and Related				
Foreclosed Property (Net) (Note 9)	4,057			
General Property Plant and Equipment (Net) (Note 10)		2		
Other Assets (Note 8)	97	422		
TOTAL ASSETS (Note 6)	$37,161	$12,135	$11,018	$11,887
LIABILITIES				
Intragovernmental Liabilities				
Accounts Payable				$4
Debt (Note 12)	$7,548			
Other Intragovernmental Liabilities (Note 13)	771		$103	$1
Total Intragovernmental Liabilities (Note 11)	$8,319		$103	$5
Accounts Payable	597	$42	6	20
Loan Guarantees Liabilities (Note 9)	4,584			
Debt Held by the Public (Note 12)	132			
Federal Employee and Veterans' Benefits (Note 2)			8	7
Debentures Issued to Claimants (Note 12)				
Loss Reserves (Note 14)		539		
Other Governmental Liabilities (Note 13)	373	461	9	6
TOTAL LIABILITIES (Note 11)	$14,005	$1,042	$126	$38
NET POSITION				
Unexpended Appropriations	$609		$10,892	$11,849
Cumulative Results of Operations	22,546	$11,093		
Total Net Position	$23,156	$11,093	$10,892	$11,849
Total Liabilities and Net Position	$37,161	$12,135	$11,018	$11,887

Figures may not add to totals because of rounding.

Consolidating Balance Sheet
As of September 2005
(Dollars in millions)

	HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
	$5,875	$875	$8,683	$6,867	$9,205		$67,500
							30,715
	6	16	27	1	(93)		28
	$5,881	$891	$8,710	$6,869	$9,112		$98,243
							201
			1		4		646
			1	6,560	200		10,818
					139		141
					1		520
	$5,881	$891	$8,712	$13,429	$9,457		$110,569
					($4)		
			$1,090	$285			$8,922
	$1	$1			117		995
	$1	$1	$1,090	$285	$113		$9,917
	12	114	15	5	36		847
					94		4,678
			1,410				1,542
	3	5	2	2	56		82
							539
	3	6	2	21	133		1,014
	$18	$126	$2,519	$313	$433		$18,619
	$5,863	$764	$8,562	$6,830	$8,458		$53,828
			(2,369)	6,286	566		38,122
	$5,863	$764	$6,193	$13,116	$9,024		$91,950
	$5,881	$891	$8,712	$13,429	$9,457		$110,569

Consolidating Balance Sheet
As of September 2004
(Dollars in millions)

	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
ASSETS				
Intragovernmental				
Fund Balance with Treasury (Note 3)	$7,898	$3,355	$12,889	$12,040
Investments (Note 5)	23,430	7,599		
Accounts Receivable (Note 7)				
Other Assets (Note 8)	64		4	9
Total Intragovernmental Assets (Note 6)	$31,392	$10,954	$12,893	$12,049
Investments (Net) (Note 5)	122			
Accounts Receivable (Net) (Note 7)	234	25	229	
Credit Program Receivables and Related				
Foreclosed Property (Net) (Note 9)	3,947			
General Property Plant and Equipment (Net) (Note 10)		4		
Other Assets (Note 8)	120	428		
TOTAL ASSETS (Note 6)	$35,815	$11,411	$13,122	$12,049
LIABILITIES				
Intragovernmental Liabilities				
Accounts Payable				
Debt (Note 12)	$7,635			
Other Intragovernmental Liabilities (Note 13)	627		$132	$1
Total Intragovernmental Liabilities (Note 11)	$8,262		$132	$5
Accounts Payable	533	40	15	19
Loan Guarantees Liabilities (Note 9)	5,074			
Debt Held by the Public (Note 12)	187			
Federal Employee and Veterans' Benefits(Note 2)			8	7
Debentures Issued to Claimants (Note 12)				
Loss Reserves (Note 14)		519		
Other Governmental Liabilities (Note 13)	590	465	9	6
TOTAL LIABILITIES (Note 11)	$14,646	$1,024	$164	$37
NET POSITION				
Unexpended Appropriations	$699		$12,958	$12,011
Cumulative Results of Operations	20,470	$10,388		
Total Net Position	$21,169	$10,388	$12,958	$12,011
Total Liabilities and Net Position	$35,815	$11,411	$13,122	$12,049

Figures may not add to totals because of rounding.

Consolidating Balance Sheet
As of September 2004
(Dollars in millions)

HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
$5,703	$2,010	$8,789	$7,160	$9,803		$69,647
						31,029
2	9	30	1	(100)		21
$5,706	$2,019	$8,819	$7,162	$9,704		$100,697
						122
				4		491
		2	7,082	206		11,238
				91		96
				2		550
$5,706	$2,019	$8,822	$14,244	$10,007		$113,194
				($4)		
		$1,183	$1,284			10,102
	$1			28		790
	$1	$1,183	$1,285	$24		$10,892
10	135	28	4	33		817
				97		5,172
		1,670				1,858
3	5	2	2	53		79
						519
3	6	2	20	98		1,199
$16	$147	$2,885	$1,311	$305		$20,536
$5,689	$1,872	$8,647	$7,060	$9,195		$58,131
		(2,710)	5,872	507		34,527
$5,689	$1,872	$5,936	$12,933	$9,702		$92,658
$5,706	$2,019	$8,822	$14,244	$10,007		$113,194

Consolidating Statement of Net Cost
For the Period Ended September 2005 and 2004
(Dollars in millions)

2005	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
PROGRAM COSTS				
Intragovernmental Gross Costs	$532		$65	$23
Less: Intragovernmental Earned Revenue	(1,491)	($457)		
Intragovernmental Net Costs	($959)	($457)	$65	$23
Gross Costs With the Public	$254	$81	$23,330	$5,002
Less: Earned Revenues	(363)	(329)		
Net Costs With the Public	($109)	($248)	$23,330	$5,002
Total Net Costs	($1,068)	($705)	$23,395	$5,025
Costs Not Assigned to Programs				
Net Cost of Operations	($1,068)	($705)	$23,395	$5,025

2004	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
PROGRAM COSTS				
Intragovernmental Gross Costs	$719		$64	$38
Less: Intragovernmental Earned Revenue	(1,552)	($443)		
Intragovernmental Net Costs	($832)	($443)	$64	$38
Gross Costs With the Public	($667)	$78	$22,401	$5,419
Less: Earned Revenues	(250)	(373)		
Net Costs With the Public	($917)	($295)	$22,401	$5,419
Total Net Costs	($1,750)	($738)	$22,465	$5,457
Costs Not Assigned to Programs				
Net Cost of Operations	($1,750)	($738)	$22,465	$5,457

Figures may not add to totals because of rounding.

Consolidating Statement of Net Cost
For the Period Ended September 2005 and 2004
(Dollars in millions)

HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
$20	$12	$176	$115	$204		$1,147
				(9)		(1,957)
$20	$12	$176	$115	$195		($810)
$1,734	$3,555	$3,425	$1,255	$3,580		$42,216
			(553)	(24)		(1,269)
$1,734	$3,555	$3,425	$702	$3,556		$40,947
$1,754	$3,567	$3,601	$817	$3,751		$40,137
				$268		$268
$1,754	$3,567	$3,601	$817	$4,019		$40,405

HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
$13	$16	$189	$183	$164		$1,384
				(5)		(1,999)
$13	$16	$189	$183	$158		($615)
$1,612	$3,449	$3,711	$1,116	$3,415		$40,534
			(616)	(32)		(1,271)
$1,612	$3,449	$3,711	$500	$3,383		$39,263
$1,625	$3,465	$3,900	$683	$3,541		$38,648
				392		392
$1,625	$3,465	$3,900	$683	$3,933		$39,040

Consolidating Statement of Changes in Net Position
For the Period Ended September 2005
(Dollars in millions)

Cumulative Results of Operations

2005	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
Net Position-Beginning of Period	($20,470)	($10,388)		
Adjustments				
Changes in Accounting Principles				
Corrections of Errors				
Beginning Balances, As Adjusted	($20,470)	($10,388)		
Budgetary Financing Sources				
Appropriations Used	($1,859)		($23,274)	($4,984)
Transfers In/Out Without Reimbursement	576			
Other Budgetary Financing Sources			($121)	($41)
Other Financing Sources				
Transfers In/Out Without Reimbursement	297			
Imputed Financing from Costs Absorbed by Others	($23)			
Other				
Total Financing Sources	($1,008)		($23,395)	($5,025)
Net Cost of Operations	(1,068)	(705)	23,395	5,025
Net Change	(2,076)	(705)		
Ending Balances	($22,546)	($11,093)		

Unexpended Appropriations

	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
Net Position-Beginning of Period	($699)		($12,958)	($12,011)
Adjustments				
Changes in Accounting Principles				
Corrections of Errors				
Beginning Balances, As Adjusted	($699)		($12,958)	($12,011)
Budgetary Financing Sources				
Appropriations Received	($1,987)		($22,726)	($4,891)
Transfers In/Out	137			(1)
Other Adjustments (Rescissions, etc)	81		1,518	70
Appropriations Used	1,859		23,274	4,984
Total Financing Sources	$89		$2,066	$162
Ending Balances	($609)		($10,892)	($11,849)

Figures may not add to totals because of rounding.

Consolidating Statement of Changes in Net Position
For the Period Ended September 2005
(Dollars in millions)

HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
		$2,710	($5,872)	($507)		($34,527)
		$2,710	($5,872)	($507)		($34,527)
($1,716)	($3,545)	($3,886)	($1,213)	($4,131)		($44,607)
			28	(220)		384
($38)	($22)	($56)	($44)	323		
				7		304
				(58)		(81)
($1,754)	($3,567)	($3,942)	($1,230)	($4,077)		($44,000)
1,754	3,567	3,601	817	4,019		40,405
		(341)	(413)	(59)		(3,595)
		$2,369	($6,286)	($566)		($38,122)

HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
($5,689)	($1,872)	($8,647)	($7,060)	($9,194)		($58,131)
($5,689)	($1,872)	($8,647)	($7,060)	($9,195)		($58,131)
($1,915)	($2,458)	($3,825)	($1,225)	($3,610)		($42,637)
				(9)		127
25	21	23	242	225		2,206
1,716	3,545	3,886	1,213	4,131		44,607
($174)	$1,107	$84	$230	$737		$4,303
($5,863)	($764)	($8,562)	($6,830)	($8,458)		($53,828)

Consolidating Statement of Changes in Net Position
For the Period Ended September 2004
(Dollars in millions)

Cumulative Results of Operations

2004 Restated	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
Net Position-Beginning of Period	($17,659)	($9,650)		
Prior Period Adjustments (Note 19)				
Beginning Balances, As Adjusted	($17,659)	($9,650)		
Budgetary Financing Sources				
Other Adjustments (Rescissions, etc)				
Appropriations Used	($1,812)		($22,362)	($5,394)
Transfers In/Out Without Reimbursement	555			
Other Budgetary Financing Sources			(103)	(63)
Other Financing Sources				
Donations and Forfeitures of Property				
Transfers In/Out Without Reimbursement	208			
Imputed Financing From Costs Absorbed From Others	(14)			
Other	2			
Total Financing Sources	($1,061)		($22,465)	($5,457)
Net Cost of Operations	(1,750)	(738)	22,465	5,457
Ending Balances	($20,470)	($10,388)		

Unexpended Appropriations

	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
Net Position-Beginning of Period	($576)		($19,040)	($12,488)
Prior Period Adjustments				
Beginning Balances, As Adjusted	($576)		($19,040)	($12,488)
Budgetary Financing Sources				
Appropriations Received	($2,023)		($19,371)	($4,964)
Transfers In/Out	84			2
Other Adjustments (Rescissions, etc)	5		3,095	50
Appropriations Used	1,812		22,358	5,388
Total Financing Sources	($122)		$6,082	$477
Ending Balances	($699)		($12,958)	($12,011)

Figures may not add to totals because of rounding.

Consolidating Statement of Changes in Net Position
For the Period Ended September 2004
(Dollars in millions)

HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
		$3,056	($5,453)	($459)		($30,166)
				5		5
		$3,056	($5,453)	($454)		($30,161)
($1,607)	($3,439)	($4,185)	($1,095)	($3,966)		($43,859)
			25	(274)		306
(18)	(26)	(60)	(33)	301		(2)
				1		209
				(49)		(62)
						2
($1,625)	($3,465)	($4,245)	($1,102)	($3,987)		($43,406)
1,625	3,465	3,899	683	3,933		39,040
		$2,710	($5,872)	($507)		($34,527)

HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
($5,291)	($1,734)	($8,928)	($7,132)	($9,564)		($64,753)
($5,291)	($1,734)	($8,928)	($7,132)	($9,564)		($64,753)
($2,018)	($3,600)	($3,894)	($1,029)	($3,670)		($40,569)
				(1)		85
20	21	22	6	63		3,281
1,600	3,441	4,154	1,095	3,977		43,825
($398)	($138)	$281	$72	$369		$6,622
($5,689)	($1,872)	($8,647)	($7,060)	($9,195)		($58,131)

Combining Statement of Budgetary Resources
For the Period Ended September 2005
(Dollars in millions)

	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants	HOME	Operating Subsidies
Budgetary Resources:						
Appropriations Received	$1,987		$22,726	$4,891	$1,915	$2,458
Borrowing Authority	(9)					
Contract Authority						
Net Transfers		$11		(1)		
Other						
Unobligated Balance						
Beginning of Period	23,978	10,841	2,254	1,346	457	3
Net Transfers, Actual		208		2		
Anticipated Transfers, Balances						
Spending Authority from Offsetting Collections						
Earned						
Collected	2,757	640		2		
Receivable from Federal Sources	13					
Change in Unfilled Customer Orders						
Advance Received						
W/O Advance from Federal Sources						
Anticipated for Rest of Year						
Anticipated for Rest of Year, w/o Advance						
Transfers from Trust Funds						
Collected						
Anticipated						
Subtotal	$2,770	$640		$2		
Recoveries of Prior Year Adjustments						
Actual Recoveries	20		1,454	28	6	2
Anticipated Recoveries						
Temporarily Not Available Per PL						
Permanently not available						
Cancellations-Expired and No Year Accts	(45)			(32)	(10)	
Enacted Rescissions	(36)		(1,618)	(38)	(15)	(21)
Capital Trans & Debt Redemption	(230)					
Other Authority Withdrawn			(31)			
Pursuant to Public Law			(2,500)			
Anticipated for Rest of Year						
Total Budgetary Resources	$28,435	$11,699	$22,286	$6,199	$2,353	$2,442

Combining Statement of Budgetary Resources
For the Period Ended September 2005
(Dollars in millions)

	Public and Indian Housing Loans & Grants	Housing for the Elderly and Disabled	All Other	2003 Budgetary Total	Federal Housing Administration Non-Budgetary	Other Non Budgetary Credit Program Accounts	2003 Total Non-Budgetary Credit Program Financing Accounts	Total
	$3,825	$1,225	$3,619	$42,647				$42,647
	20			11	$1,174		$1,174	1,186
			757	757				757
			11	21				21
	398	1,664	3,791	44,731	4,608	114	4,723	49,454
			(2)	208				208
	84	1,059	700	5,242	11,722	18	11,740	16,983
				12	(86)		(86)	(74)
			66	66				66
			(8)	(7)		3	3	(4)
	$84	$1,059	$759	$5,314	$11,635	$22	$11,657	$16,971
	22	24	439	1,996	39		39	2,035
			(43)	(130)				(130)
	(26)	(246)	(274)	(2,274)				(2,274)
	(100)	(991)	(13)	(1,335)	(1,214)		(1,214)	(2,549)
	(8)		(638)	(677)				(677)
	(600)		(626)	(3,726)				(3,726)
	$3,614	$2,735	$7,780	$87,542	$16,243	$136	$16,379	$103,922

Combining Statement of Budgetary Resources
For the Period Ended September 2005
(Dollars in millions)

	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants	HOME	Operating Subsidies
Status of Budgetary Resources:						
Obligations Incurred						
Category A Direct						
Category B Direct	4,833	120	20,175	4,980	2,035	2,440
Exempt from Apportionment						
Unobligated Balances Available						
Balance, Currently Available	77	0	2,035	1,183	318	0
Apportioned for Subsequent Periods						
Anticipated						
Exempt from Apportionment						
Other Available						
Unobligated Balances Not Available						
Deferred						
Withheld Pending Rescission		11,579				
Other	23,525		76	36		2
Total Status of Budgetary Resources	$28,435	$11,699	$22,286	$6,199	$2,353	$2,442
Relationship of Obligations to Outlays						
Obligated Balance, Net-Beg of Period	$743	$36	$26,383	$10,694	$5,247	$2,007
Obligated Balance Transferred, Net						
Less: Obligated Balance, Net - End of Period						
Accounts Receivable	($261)	($78)				
Unfilled Customer Orders from Fed Source						
Undelivered Orders	552		21,816	10,635	5,546	759
Accounts Payable	515	121	4	23	11	113
Outlays						
Disbursements	$4,737	$112	$23,284	$4,987	$1,718	$3,572
Collections	(2,757)	(640)		(2)		
Subtotal	$1,980	($528)	$23,284	$4,984	$1,718	$3,572
Less: Offsetting Receipts	(474)					
Net Outlays	$1,507	($528)	$23,284	$4,984	$1,718	$3,572

Combining Statement of Budgetary Resources
For the Period Ended September 2005
(Dollars in millions)

Public and Indian Housing Loans & Grants	Housing for the Elderly and Disabled	All Other	2003 Budgetary Total	Federal Housing Administration Non-Budgetary	Other Non Budgetary Credit Program Accounts	2003 Total Non-Budgetary Credit Program Financing Accounts	Total
		$1,263	$1,263				$1,263
3,213	1,398	3,697	42,890	10,352	21	10,373	53,264
384	1,320	2,407	7,723	2,649	13	2,662	10,385
			11,579				11,579
17	17	414	24,087	3,242	102	3,344	27,431
$3,614	$2,735	$7,780	$87,542	$16,243	$136	$16,379	$103,922
$11,139	$5,496	$13,454	$75,198	$1,125	($17)	$1,108	$76,306
		(4)	(343)	($47)		(47)	($390)
		(3)	(3)	(5)	(20)	(25)	(28)
10,268	5,480	13,098	68,154	571		571	68,725
153	50	87	1,077	692		692	1,769
$3,909	$1,340	$4,805	$48,465	$10,314	$21	$10,334	$58,800
(84)	(1,059)	(766)	(5,308)	(11,722)	(18)	(11,740)	(17,049)
$3,826	$281	$4,039	$43,157	($1,408)	$3	($1,406)	$41,751
		(9)	(483)				(483)
$3,826	$281	$4,029	$42,674	($1,408)	$3	($1,406)	$41,268

Combining Statement of Budgetary Resources
For the Period Ended September 2004
(Dollars in millions)

	Federall Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants	HOME	Operating Subsidies
Budgetary Resources:						
Appropriations Received	$2,023		$19,371	$4,964	$2,018	$3,600
Borrowing Authority	130					
Contract Authority						
Net Transfers		11		(2)		
Other						
Unobligated Balance						
Beginning of Period	27,111	10,106	3,483	1,146	388	2
Net Transfers, Actual		394				
Anticipated Transfers, Balances						
Spending Authority from Offsetting Collections						
Earned						
Collected	4,432	443				
Receivable from Federal Sources	(30)					
Change in Unfilled Customer Orders						
Advance Received						
W/O Advance from Federal Sources						
Anticipated for Rest of Year						
Anticipated for Rest of Year, w/o Advance						
Transfers from Trust Funds						
Collected						
Anticipated						
Subtotal	$4,403	$443				
Recoveries of Prior Year Adjustments						
Actual Recoveries	37		1,655	20	16	1
Anticipated Recoveries						
Temporarily Not Available Per PL						
Permanently not available						
Cancellations-Expired and No Year Accts				(14)		
Enacted Rescissions			(2,958)	(29)	(12)	(21)
Capital Trans & Debt Redemption	(294)					
Other Authority Withdrawn			(5)			
Pursuant to Public Law	(5)					
Anticipated for Rest of Year						
Total Budgetary Resources	$33,405	$10,953	$21,547	$6,084	$2,409	$3,582

Combining Statement of Budgetary Resources
For the Period Ended September 2004
(Dollars in millions)

Public and Indian Housing Loans & Grants	Housing for the Elderly and Disabled	Financial Statement Eliminations	All Other	2004 Budgetary Total	Federal Housing Administration Non Budgetary	Other Non Budgetary Credit Program Accounts	2004 Total Non-Budgetary Credit Program Financing Accounts	Total
$3,894	$1,029		$3,679	$40,577				$40,577
20				150	3,400		3,400	3,550
			495	495				495
			1	10				10
842	2,505		4,304	49,888	1,061	83	1,144	51,032
				394				394
79	1,044		703	6,700	17,303	43	17,345	24,046
		6	(2)	(25)	119		119	94
			128	128				128
			(4)	(4)	5	(3)	2	(1)
$78	$1,044	$6	$826	$6,800	$17,427	$39	$17,466	$24,266
36	24		308	2,096	12		12	2,107
			(37)	(50)				(50)
(20)	(6)		(48)	(3,094)				(3,094)
(97)	(1,462)		(12)	(1,865)	(4,559)		(4,559)	(6,424)
(21)			(82)	(108)				(108)
(530)			(676)	(1,211)				(1,211)
$4,203	$3,133	$6	$8,760	$94,083	$17,341	$122	$17,463	$111,546

Combining Statement of Budgetary Resources
For the Period Ended September 2004
(Dollars in millions)

	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants	HOME	Operating Subsidies
Status of Budgetary Resources:						
Obligations Incurred						
Category A Direct						
Category B Direct	9,427	113	19,293	4,738	1,953	3,579
Exempt from Apportionment						
Unobligated Balances Available						
Balance, Currently Available	152	0	1,563	1,307	444	2
Apportioned for Subsequent Periods						
Anticipated						
Exempt from Apportionment						
Other Available						
Unobligated Balances Not Available						
Deferred						
Withheld Pending Rescission						
Other	23,826	10,841	691	39	12	1
Total Status of Budgetary Resources	$33,405	$10,953	$21,547	$6,084	$2,409	$3,582
Relationship of Obligations to Outlays						
Obligated Balance, Net-Beg of Period	$938	$27	$31,108	$11,375	$4,917	$1,863
Obligated Balance Transferred, Net						
Less: Obligated Balance, Net - End of Period						
Accounts Receivable	($248)	($84)				
Unfilled Customer Orders from Fed Source						
Undelivered Orders	537		26,371	10,671	5,237	1,873
Accounts Payable	454	120	13	22	10	134
Outlays						
Disbursements	$9,615	$104	$22,362	$5,400	$1,607	$3,434
Collections	(4,432)	(443)		0		
Subtotal	$5,183	($339)	$22,362	$5,400	$1,607	$3,434
Less: Offsetting Receipts	(419)					
Net Outlays	$4,764	($339)	$22,362	$5,400	$1,607	$3,434

Figures may not add to totals because of rounding.

Combining Statement of Budgetary Resources
For the Period Ended September 2004
(Dollars in millions)

Public and Indian Housing Loans & Grants	Housing for the Elderly and Disabled	Financial Statement Eliminations	All Other	2004 Budgetary Total	Federal Housing Administration Non Budgetary	Other Non Budgetary Credit Program Accounts	2004 Total Non-Budgetary Credit Program Financing Accounts	Total
			$1,251	1,251				$1,251
3,805	1,469	6	3,718	48,101	12,732	8	12,740	60,841
390	1,618		2,230	7,707	2,586	2	2,589	10,295
	15			15				15
8	31		1,561	37,010	2,022	112	2,134	39,144
$4,203	$3,133	$6	$8,760	$94,083	$17,341	$122	$17,463	$111,546
$11,595	$5,338	$13	$13,490	$80,663	$941	($20)	$921	$81,584
			($5)	($337)	($133)		($133)	($470)
			(11)	(11)	(5)	(17)	(22)	(33)
10,962	5,411		13,386	74,448	520		520	74,968
177	85		82	1,096	744		744	1,840
$4,225	$1,287	$13	$4,703	$52,749	$12,412	$8	$12,420	$65,169
(78)	(1,044)		(831)	(6,828)	(17,303)	(43)	(17,345)	(24,173)
$4,147	$243	$13	$3,872	$45,921	($4,891)	($35)	($4,926)	$40,996
			(9)	(428)				(428)
$4,147	$243	$13	$3,863	$45,493	($4,891)	($35)	($4,926)	$40,568

Consolidating Statement of Financing
For the Year Ended September 2005
(Dollars in millions)

	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
Resources Used to Finance Activities:				
Budgetary Resources Obligated				
Obligations Incurred	$15,185	$120	$20,175	$4,980
Less: Spending Authority from Offsetting				
Collections & Recoveries	(14,464)	(640)	(1,454)	(31)
Obligations Net of Offsetting Collections	$721	($520)	$18,721	$4,949
Less: Offsetting Receipts	(474)			
Net Obligations	$247	($520)	$18,721	$4,949
Other Resources				
Donations & Forfeitures of Property				
Transfers In/Out Without Reimbursement	($297)	($208)		
Imputed Financing from Costs Absorbed by Others				
Other Resources	23	$23		
Net Other Resources Used to Finance Activities	($274)	($185)		
Total Resources Used to Finance Activities	($27)	($705)	$18,721	$4,949
Resources Used to Finance Items Not				
Part of the Net Cost of Operations				
Change in Budgetary Resources Obligated for Goods				
Services/Benefits Ordered but not yet Provided	($56)		$4,553	$35
Resources That Fund Expenses from Prior Periods	(3,161)			
Budgetary Offsetting Collections and Receipts				
Not Affecting Net Cost of Operations	13,158			
Resources Financing Acquisition of Assets	(10,115)			
Other Changes to Net Obligated Resources				
Not Affecting Net Cost of Operations	(398)		121	41
Total Resources Used to Finance Items				
Not Part of the Net Cost of Operations	($572)		$4,675	$76
Total Resources Used to Finance				
the Net Cost of Operations	($598)	($705)	$23,395	$5,025

Consolidating Statement of Financing
For the Year Ended September 2005
(Dollars in millions)

HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
$2,035	$2,440	$3,213	$1,398	$4,981		$54,526
(6)	(2)	(106)	(1,083)	(1,219)		(19,006)
$2,029	$2,438	$3,107	$315	$3,762		$35,520
				(9)		(483)
$2,029	$2,438	$3,107	$315	$3,752		$35,037
				($7)		($512)
				58		58
			$5	1		53
			$5	$52		(401)
$2,029	$2,438	$3,107	$320	$3,804		$34,636
($312)	$1,107	$697	($69)	$357		$6,312
		(1)				(3,162)
			1,059	45		14,262
		83	12	(83)		(10,103)
38	22	(286)	44	(84)		(501)
($274)	$1,129	$493	$1,046	$235		$6,808
$1,754	$3,567	$3,600	$1,365	$4,040		$41,444

Consolidating Statement of Financing
For the Year Ended September 2005
(Dollars in millions)

	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
Components of Net Cost of Operations Not Requiring/Generating Resources in the Current Period:				
Components Requiring or Generating Resources in Future Periods				
Increase in Annual Leave Liability (Note 22)				
Increase in Environmental/Disposal Liability				
Reestimates of Credit Subsidy Expense	$2,150			
Exchange Revenue Receivable from the Public				
Other				
Total Requiring/Generating Resources in Future Periods	$2,150			
Components Not Requiring/Generating Resources				
Depreciation and Amortization				
Revaluation of Assets or Liabilities	($1,337)			
Other	(1,283)			
Total Components of Net Cost of Operation Not Requiring/Generating Resources	($2,619)			
Total Components of Net Cost of Operations Not Requiring/Generating Resources in the Current Period	($470)			
Net Cost of Operations	($1,068)	($705)	$23,395	$5,025

Figures may not add to totals because of rounding.

Consolidating Statement of Financing
For the Year Ended September 2005
(Dollars in millions)

HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
				$2		$2
				0		0
				(19)		2,131
			($554)	(9)		(563)
				3		3
			($554)	($23)		$1,573
				$15		$15
				(1)		(1,338)
		$1	5	(12)		(1,289)
		$1	$5	$2		($2,612)
		$1	($549)	($21)		($1,039)
$1,754	$3,567	$3,601	$817	$4,019		$40,405

Consolidating Statement of Financing
For the Year Ended September 2004
(Dollars in millions)

	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
Resources Used to Finance Activities:				
Budgetary Resources Obligated				
Obligations Incurred	$22,159	$113	$19,293	$4,738
Less: Spending Authority from Offsetting Collections & Recoveries	(21,878)	(443)	(1,655)	(19)
Obligations Net of Offsetting Collections	$281	($330)	$17,637	$4,719
Less: Offsetting Receipts	(419)			
Net Obligations	($138)	($330)	$17,637	$4,719
Other Resources				
Donations & Forfeitures of Property				
Transfers In/Out Without Reimbursement	($208)	($394)		
Imputed Financing from Costs Absorbed by Others	14			
Other Resources	(2)	(13)		
Net Other Resources Used to Finance Activities	($196)	($408)		
Total Resources Used to Finance Activities	($334)	($738)	$17,637	$4,719
Resources Used to Finance Items Not Part of the Net Cost of Operations				
Change in Budgetary Resources Obligated for Goods Services/Benefits Ordered but not yet Provided	($340)		$4,725	$675
Resources That Fund Expenses from Prior Periods	(7,546)			
Budgetary Offsetting Collections and Receipts Not Affecting Net Cost of Operations	20,097			
Resources Financing Acquisition of Assets	(12,630)			
Other Changes to Net Obligated Resources Not Affecting Net Cost of Operations	138		103	63
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	($281)		$4,828	$738
Total Resources Used to Finance the Net Cost of Operations	($615)	($738)	$22,465	$5,457

Consolidating Statement of Financing
For the Year Ended September 2004
(Dollars in millions)

HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
$1,953	$3,579	$3,805	$1,469	$4,977	$6	$62,091
(16)	(1)	(114)	(1,067)	(1,173)	(6)	(26,373)
$1,937	$3,579	$3,691	$402	$3,803		$35,718
				(9)		(428)
$1,937	$3,579	$3,691	$402	$3,794		$35,290
				($1)		($604)
				49		63
				(6)		(21)
				$41		$ (562)
$1,937	$3,579	$3,691	$402	$3,835		$34,728
($330)	($139)	$416	($188)	$102		$4,921
				(1)		(7,548)
			1,041	65		21,203
		78		(43)		(12,595)
18	26	(286)	33	(25)		71
($312)	($114)	$209	$886	$98		$6,052
$1,625	$3,465	$3,899	$1,287	$3,933		$40,780

Consolidating Statement of Financing
For the Year Ended September 2004
(Dollars in millions)

	Federal Housing Administration	Government National Mortgage Association	Section 8 Rental Assistance	Community Development Block Grants
Components of Net Cost of Operations Not Requiring/Generating Resources in the Current Period:				
Components Requiring or Generating Resources in Future Periods				
Increase in Annual Leave Liability (Note 22)				
Increase in Environmental/Disposal Liability				
Reestimates of Credit Subsidy Expense	2,866			
Exchange Revenue Receivable from the Public				
Other				
Total Requiring/Generating Resources in Future Periods	$2,866			
Components Not Requiring/Generating Resources				
Depreciation and Amortization				
Revaluation of Assets or Liabilities	($1,433)			
Other	(2,569)			
Total Components of Net Cost of Operations Not Requiring/Generating Resources	($4,002)			
Total Components of Net Cost of Operations Not Requiring/Generating Resources in the Current Period	($1,135)			
Net Cost of Operations	($1,750)	($738)	$22,465	$5,457

Figures may not add to totals because of rounding.

Consolidating Statement of Financing
For the Year Ended September 2004
(Dollars in millions)

HOME	Operating Subsidies	Public and Indian Housing Loans and Grants	Housing for the Elderly and Disabled	All Other	Financial Statement Eliminations	Consolidating
				3		3
				(7)		2,859
			(605)	(10)		(615)
				(5)		(5)
			($605)	($20)		$2,242
				$14		$14
						(1,433)
				6		(2,563)
				$20		($3,982)
			($605)			($1,740)
$1,625	$3,465	$3,899	$683	$3,933		$39,040

Required Supplementary Stewardship Information

This section provides information on resources entrusted to HUD that do not meet the criteria for information required to be reported or audited in HUD's financial statements but are, nonetheless, important to understand HUD's operations and financial conditions. The stewardship objective requires that HUD report on the broad outcomes of its actions associated with these resources. Such reporting will provide information that will help report users assess the impact of HUD's operations and activities.

HUD's stewardship reporting responsibilities extend to the investments made by a number of HUD programs in Non-Federal Physical Property, Human Capital, and Research and Development. Due to the relative immateriality of the calculations and in the application of the related administrative costs, most of the amounts reported below reflect direct program costs only. The investments addressed in this section are attributable to programs administered through the following offices:

- Community Planning and Development (CPD);
- Public and Indian Housing (PIH);
- Policy Development and Research; and
- Healthy Homes and Lead Hazard Control.

Overview of HUD's Major Programs

CPD seeks to develop viable communities by promoting integrated approaches that provide decent housing, a suitable living environment, and expanded economic opportunities for low- and moderate-income persons. HUD makes stewardship investments through the following CPD programs:

- **Community Development Block Grants (CDBG)** are provided to state and local communities, which use these funds to support a wide variety of community development activities within their jurisdiction. These activities are designed to benefit low- and moderate-income persons, aid in the prevention of slums and blight, and meet other urgent community development needs. State and local communities use the funds as they deem necessary, as long as the use of these funds meets at least one of these objectives. A portion of the funds supports the acquisition or rehabilitation of property owned by state and local governments, while other funds help to provide employment and job training to low and moderate-income persons.
- **Disaster Grants** help state and local governments recover from major natural disasters. A portion of these funds can be used to acquire, rehabilitate, or demolish physical property.
- **HOME Investment Partnerships** provide formula grants to states and localities (used often in partnership with local nonprofit groups) to fund a wide range of activities that build, buy, and/or rehabilitate affordable housing for low-income persons.
- **Youthbuild** grants assist young individuals to obtain education, employment skills, and meaningful work experience in the construction trade, enabling them to become more productive and self-sufficient.

PIH ensures safe, decent, and affordable housing, creates opportunities for residents' self-sufficiency and economic independence, and assures the fiscal integrity of all program participants. HUD makes stewardship investments through the following PIH programs:

- The **Public Housing Capital Fund** provides grants to PHAs to improve the physical conditions and to upgrade the management and operation of existing public housing.
- **Neighborhood Network Initiative** grants are provided to PHAs to support the improvement of the living environment of public housing residents in distressed public housing units. Some investments support the acquisition or rehabilitation of PHA-owned property, while others help to provide education and job training to residents of the communities targeted for rehabilitation.
- **Indian Housing Block Grants** provide funds needed to allow tribal housing organizations to maintain existing units and to begin development of new units to meet their critical long-term housing needs.
- **Indian Community Development Block Grants** provide funds to Indian organizations to develop viable communities, including decent housing, a suitable living environment, and economic opportunities, principally for low- and moderate-income recipients.
- The **Public Housing Drug Elimination Program** seeks to eliminate drug-related crime and activities in public and Indian housing communities. A portion of these funds is used to improve properties owned by the PHAs and thus increase security and prevent crime at the properties. Congress terminated funding for this program after FY 2001.

The **Office of Policy Development and Research's** stewardship responsibilities include maintaining current information to monitor housing needs and housing market conditions, and to support and conduct research on priority housing and community development issues.

HUD makes stewardship investments through the following programs:

- **Community Development Work Study:** Colleges and universities throughout the United States use this program to offer financial aid and work experience to students enrolled in a full-time graduate program in community development or a closely related field such as urban planning, public policy, or public administration.
- **Partnership for Advancing Technology in Housing** is a public/private sector initiative which seeks to expand the development and utilization of new technologies in order to make American homes stronger, safer, and more durable; more energy efficient and environmentally friendly; easier to maintain and less costly to operate; and more comfortable and exciting places to live. This program links key agencies in the federal government with leaders from the home building, product manufacturing, insurance, financial, and regulatory communities in a unique partnership focused on technological innovation in the American housing industry.

The **Office of Healthy Homes and Lead Hazard Control** seeks to eliminate childhood lead poisoning caused by lead-based paint hazards and to address other children's disease and injuries, such as asthma, unintentional injury, and carbon monoxide poisoning, caused by substandard housing conditions.

- **Lead Technical Assistance Division,** in support of the Departmental lead hazard control program, establishes and coordinates lead-based paint regulations and policy, and supports compliance assistance and enforcement. These programs also support technical assistance and the conduct of technical studies and demonstrations to identify innovative methods to create lead-safe housing at reduced cost. In addition, these programs are designed to increase the awareness of lead professionals, parents, building owners, housing and public health professionals, and others with respect to lead-based paint and related property-based health issues.

Investments in Non-Federal Physical Property

Non-federal physical property investments support the purchase, construction, or major renovation of physical property owned by state and local governments. These investments support three of HUD's strategic goals: to increase the availability of decent, safe, and affordable housing in America communities; improve community quality of life and economic vitality; and ensure public trust in HUD. The following table summarizes material program investments in Non-federal physical property. Additional information regarding the following programs' contribution to HUD's goals may be found in Section 2 of this report.

Investments in Non-Federal Physical Property
FY 2001 - 2005
(Dollars in millions)

Program	2001	2002	2003	2004	2005
CPD					
CDBG	$1,189	$1,298	$1,206	$1,193	$1,175
Disaster Grants(1)	$56	$29	$7	$114	$40
HOME	$24	$8	$33	$26	$44
PIH					
Indian CDBG	$53	$51	N/A	$58	$71
Indian Housing Block Gr	N/A	$292	$296	$176	$213
HOPE VI (2)	$495	$367	$427	$411	$386
Pub Housing Cap Fund	$1,863	$2,036	$1,949	$1,758	$1,289
Drug Elim Prog (3)	$4	$0	$0	$0	$0
TOTAL	**$3,684**	**$4,081**	**$3,918**	**$3,736**	**$3,218**

Notes:
1. *Amount reported for FY 2005 represents 9 months of data.*
2. *For FY 2005, HOPE VI's 4th quarter investment amounts and results of investments were estimated based on the percentage change between FY 2004 3rd quarter and 4th quarter data.*
3. *Congress terminated funding for the Public Housing Drug Elimination Program after FY 2001.*

Investments in Human Capital

Human Capital investments support education and training programs that are intended to increase or maintain national economic productive capacity. These investments support HUD's strategic goals, which are to promote self-sufficiency and asset development of families and individuals; improve community quality of life and economic vitality; and ensure public trust in HUD. The table on the next page summarizes material program investments in Human Capital, for FY 2001 through 2005. Additional information regarding the following programs' contributions to HUD's goals may be found in Section 2 of this report.

Investments in Human Capital
FY 2001 - 2005
(Dollars in millions)

Program	2001	2002	2003	2004	2005
CPD					
CDBG	$25	$29	$23	$26	$28
Youthbuild	$15	$14	$19	$21	$22
PIH					
HOPE VI (2)	$55	$51	$56	$53	$39
Policy Dev and Research					
Comm. Dev. Work Study	$3	$3	$3	$3	$3
Healthy Homes/Lead Haz					
Lead Technical Assistance	$2	$7	$1	$0	$0
TOTAL	**$100**	**$104**	**$102**	**$103**	**$92**

Results of Human Capital Investments: The following table presents the results of or output (number of people trained) of human capital investments made by HUD's CPD, Policy Development and Research, and Healthy Homes and Lead Hazard Control programs:

Results of Investments in Human Capital
Number of People Trained
FY 2001 - 2005

Program	2001	2002	2003	2004	2005
CPD					
CDBG	127,565	149,502	172,416	131,653	122,578
Youthbuild	3,614	2,717	4,123	3,508	4,366
PIH					
HOPE VI (*see table below*)					
Policy Dev and Research					
Comm. Dev. Work Study	98	99	95	99	108
Healthy Homes/Lead Hazard					
Lead Technical Assistance	19,579	23,501	0	0	0
TOTAL	**150,856**	**175,819**	**176,634**	**135,260**	**127,052**

***HOPE VI Results of Investments in Human Capital*:** Since the inception of the HOPE VI program in FY 1993, the program has made significant investments in Human Capital related initiatives (i.e., education and training). The following table presents HOPE VI's key cumulative performance information for FY 2004 and 2005, since the program's inception.

Key Results of HOPE VI Program Activities
FY 2004 and 2005

HOPE VI Service	2004 Enrolled	2004 Completed	% Completed	2005 Enrolled	2005 Completed	% Completed
Employment Preparation, Placement, & Retention	77,146	N/A	N/A	57,424	N/A	N/A
Job Skills Training Programs	32,154	17,123	53%	22,753	12,448	55%
High School Equivalent Education	18,749	5,956	32%	12,843	3,631	28%
Entrepreneurship Training	2,536	1,094	43%	2,732	1,214	44%
Homeownership Counseling	8,361	3,354	40%	10,969	4,135	38%

Investments in Research and Development

Research and development investments support (1) the search for new knowledge, and (2) the refinement and application of knowledge or ideas, pertaining to development of new or improved products or processes. Research and development investments are intended to increase economic productive capacity or yield other future benefits. As such, these investments support HUD's strategic goals, which are to increase the availability of decent, safe, and affordable housing in America's communities; and ensure public trust in HUD. The following table summarizes HUD's research and development investments. Additional information regarding the following programs' contributions to HUD's goals may be found in Section 2 of this report.

Investments in Research and Development
FY 2001 - 2005
(Dollars in millions)

Program	2001	2002	2003	2004	2005
Policy Development and Res					
Partn. For Adv. Tech. In Hous	$9	$10	$8	$8	$8
Healthy Homes/Lead Hazard					
Lead Hazard Control	$6	$3	$9	$6	$5
TOTAL	**$15**	**$13**	**$17**	**$14**	**$13**

Results of Investments in Research and Development: At the end of FY 2005, the Partnership for Advancing Technology in Housing program had over 160 updated technology listings in its technology inventory. During FY 2005, the program awarded 10 university-based applied research projects (in partnership with the National Science Foundation), 3 technology development projects, 5 projects providing information to builders and researchers, 6 technology policy/planning research projects, and 4 projects that require demonstrations of the use of technologies.

In support of HUD's lead hazard control initiatives, the Healthy Homes and Lead Hazard Control program has conducted various studies. As indicated in the following table, such studies have contributed to an overall reduction in the per-housing unit cost of lead hazard evaluation and control efforts. These studies have also led to the identification of the prevalence of related hazards.

Per-Housing Unit Cost of Lead Hazard Evaluation and Control
FY 2001 – 2005

Program	2001	2002	2003	2004	2005
Healthy Homes/Lead Haz Cont					
Lead Hazard Control (1)	$4,639	$5,441	$4,827	$4,577	$6,650
TOTAL	**$4,639**	**$5,441**	**$4,827**	**$4,577**	**$6,650**

Notes:

1. *The FY 2005 4th quarter per-housing unit cost is based on an extrapolation of FY 2005 1st – 3rd quarter data. The Office of Healthy Homes and Lead Hazard Control anticipates that full year actual data, which becomes available the first week of November 2005, will show that the grant program will meet its goal of making 9,500 units lead safe. As a result, the Office anticipates a downward adjustment of the unit cost.*

Required Supplementary Information

Intragovernmental Balances

HUD's intragovernmental amounts represent transactions with other federal entities included in the government's annual report. These transactions include assets, liabilities and earned revenues as follows:

September 30, 2005 (dollars in millions):

Intragovernmental Assets:

Trading Partner	Fund Balance	Accounts Receivable	Investments	Other Assets	Total
Department of Treasury	$ 67,500	$ -	$ 30,715	$ -	$ 98,215
Department of Commerce	-	-	-	$ 11	$ 11
Department of Justice	-	-	-	17	$ 17
Total	$ 67,500	$ -	$ 30,715	$ 28	$ 98,243

Intragovernmental Liabilities:

Trading Partner	Accounts Payable	Debt	Other	Total
Department of Treasury	$ -	$ 8,922	$ 897	$ 9,819
Other Agencies	-	-	98	98
Total	-	$ 8,922	$ 995	$ 9,917

Intragovernmental Earned Revenues and Related Costs:

Trading Partner	Earned Revenue
Department of Treasury	$ 1,954
Other Agencies	3
Total	$ 1,957

Budget Functional Classification	Gross Cost to Generate Revenue
Commerce and Housing Credit	$ -
Community and Regional Dev	-
Income Security	-
Total	$ -

September 30, 2004 (dollars in millions) – RESTATED:

Intragovernmental Assets:

Trading Partner	Fund Balance	Accounts Receivable	Investments	Other Assets	Total
Department of Treasury	$ 69,647	$ -	$ 31,029	$ -	$ 100,676
Department of Commerce	-	-	-	12	$ 12
Department of Justice	-	-	-	9	$ 9
Total	$ 69,647	$ -	$ 31,029	$ 21	$ 100,697

Intragovernmental Liabilities:

Trading Partner	Accounts Payable	Debt	Other	Total
Department of Treasury	$ -	$ 10,102	$ 773	$ 10,875
Other Agencies	-	-	17	17
Total	-	$ 10,102	$ 790	$ 10,892

Intragovernmental Earned Revenues and Related Costs:

Trading Partner	Earned Revenue
Department of Treasury	$ 1,998
Other Agencies	1
Total	$ 1,999

Budget Functional Classification	Gross Cost to Generate Revenue
Commerce and Housing Credit	$ -
Community and Regional Dev	-
Income Security	-
Total	$ -

Required Supplementary Information

Improper Payments Reduction Activity

HUD is the first federal agency to achieve the PMA goals for reducing improper payments. During FY 2004, HUD completed its first annual improper payment risk assessment on $52.9 billion in disbursement activity the prior year (FY 2003). Over $30 billion in disbursements in 10 major program areas were determined to be at-risk of a significant improper payment level, subject to statistical sample testing and estimation of an improper payment amount. In FY 2005, HUD completed sample testing on those 10 programs and found that only 5 of the 10 program areas had a significant improper payment problem, with a combined improper payment estimate of $1.9 billion, or 3.6 percent, of total HUD payments in FY 2003. Most of that $1.9 billion improper payment estimate pertained to HUD's 3 rental housing assistance program areas, where HUD continues to make significant progress in reducing improper payments through corrective actions initiated in FY 2001. The other two areas with an improper payment problem requiring follow-up action in FY 2005 were payments in the Single Family Acquired Asset Management System and the Public Housing Capital Fund. Highlights of HUD's FY 2005 efforts to implement the Improper Payments Information Act and reduce improper payments included:

- Update of an annual risk assessment on the $54.5 billion in disbursements in the prior year, with no new "at-risk" programs identified;
- Update of sample testing of payments in the Single Family Acquired Asset Management System, found that the previously identified improper payment problem had been eliminated;
- Verification of the corrective actions taken on the specific limited causes of improper payments identified in the Public Housing Capital Fund found that the actions taken were sufficient to eliminate the improper payment problem;
- Completion of an updated measurement of gross annual improper rental assistance payments attributed to program administrator error and tenant underreporting of income showed a 61 percent reduction in the FY 2000 baseline estimate of $3.2 billion to $1.2 billion in FY 2004;
- Completion of a $214 million baseline estimate of the third and final component of improper rental housing assistance payments – "billing error" – bringing the total current improper rental assistance payment estimate to $1.4 billion; and
- Initiation of a new computer matching system for tenant income verification that has the potential to eliminate much of the remaining $1.4 billion estimate of improper rental housing assistance payments.

The Requirements

Under the Improper Payments Information Act of 2002 (Public Law 107-300) and OMB's implementing guidance, Memorandum No. M-03-13, agencies are to annually assess all programs and activities they administer and identify those that may be susceptible to significant improper payments. Where the risk of improper payments is assessed as potentially significant, agencies are required to estimate the annual amount of improper payments and report the estimates along with plans to reduce improper payments to the President and the Congress. A "significant" level of improper payments is defined by the statute as annual improper payments exceeding a $10 million dollar threshold.

An "improper payment" is defined as any payment that should not have been made or that was made in an incorrect amount under statutory, contractual, administrative, or other legally applicable requirement. Incorrect amounts are overpayments and underpayments. An improper payment includes any payment that was made to an ineligible recipient or for an ineligible service. Improper payments are also duplicate payments, payments for services not received, and payments that do not account for credit for applicable discounts. In addition to identifying substantive errors that might warrant repayment, HUD's statistical sampling of support for payments also considered "process" errors that increase the risk of substantive payment errors, and process errors are included in HUD's improper payment estimates.

HUD's Commitment

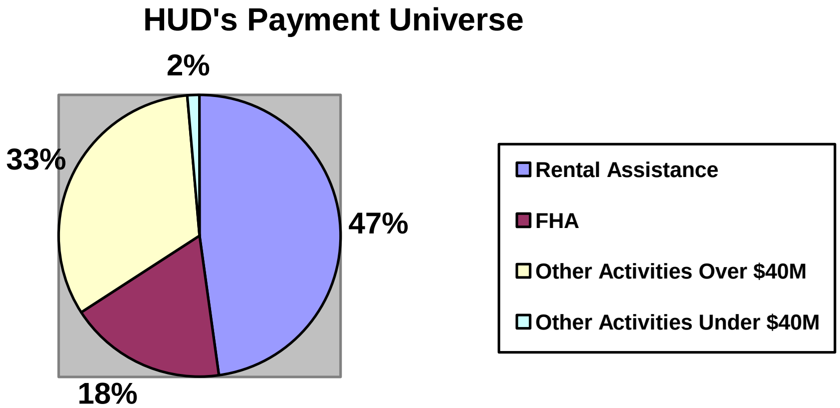
The Secretary designated the Chief Financial Officer as the lead official for directing and overseeing HUD actions to address improper payment issues and bring HUD into compliance with the requirements of the Improper Payments Information Act of 2002 and OMB Memorandum No. M-03-13. The Office of the Chief Financial Officer developed a plan for implementing the Act, and after necessary contract support services were put in place by the Chief Financial Officer and FHA, HUD began to execute the plan in FY 2004. HUD's plans, goals and results for identifying and reducing improper payments are tracked under the President's Management Agenda.

HUD's Process

The HUD process for complying with the Improper Payments Information Act consists of four steps. The first step is an initial survey of all program and administrative activities, regardless of size, for potential indicators of significant improper payments. Any program activities identified in the survey and all program activities with annual expenditures in excess of $40 million are subjected to the second step, which is a detailed risk assessment. The third step consists of statistical sample testing of payments by independent reviewers to determine the estimated amount of improper payments in any program activity determined to be susceptible to a significant improper payment level. The fourth step is to establish, execute, and monitor corrective action plans for reducing improper payments in the identified at-risk programs.

Results of Annual Risk Assessments and Continued Payment Testing

The second annual improper payment risk assessment completed during FY 2005 was based on payment and other relevant activity that occurred during the completed FY 2004 accounting cycle. An inventory of 220 distinct program and administrative payment activities was identified from all of HUD's financial management systems in FY 2004, with total payments of $54.5 billion distributed as follows:



HUD's second risk assessment fully considered the results of the first risk assessment and the outcomes of the statistical sample testing or other reviews of payments in the 10 activities the first risk assessment identified as potentially susceptible to a significant level of improper payments.

HUD's risk assessment update in FY 2005 did not identify any new activities as being at-risk of a significant improper payment level. The following chart provides a summary of the disposition or status of the 10 HUD programs that the FY 2004 risk assessment deemed to be potentially susceptible to a significant improper payment level, pending statistical sample testing. Independent reviewers performed statistical sample testing of payment activity in these 10 at-risk areas in accordance with OMB sampling guidance. Programs that tested below the improper payment threshold established by the Improper Payments Information Act were removed from HUD's at-risk inventory and are not subject to re-testing unless there is significant change in the nature of the activity or HUD's internal control structure.

FY 2004 and FY 2005 Testing Activities/Results on Inventory of Programs Assessed as "At-Risk" of a Significant Improper Payment Level		
Inventory of At-Risk Programs Selected for Statistical Sampling	**FY 2004 Testing Activity/Results**	**FY 2005 Testing Activity/Results**
FHA Payment Systems		
Single Family Acquired Asset Management System	Above Threshold – Based on completed testing of FY 2003 payments	Below Threshold – Based on completed testing of FY 2004 payments – Removed
Multifamily Property Management System	Below Threshold – Based on completed testing of FY 2003 payments – Removed	Not Applicable – Annual payment level also fell below $20 million in FY 2005
Other HUD Programs and Administrative Activities		
HOME Investment Partnerships: HOME States & Local Governments	Testing of FY 2003 payments in process	Below Threshold – Based on completed testing of FY 2003 payments – Removed
CDBG Economic Development Initiative – Special Projects	Testing of FY 2003 payments in process	Below Threshold – Based on completed testing of FY 2003 payments – Removed

Homeless Assistance Grants: Supportive Housing Program	Testing of FY 2003 payments in process	Below Threshold – Based on completed testing of FY 2003 payments – Removed
HOPE VI – Revitalization Grants	Testing of FY 2003 payments in process	Below Threshold – Based on completed testing of FY 2003 payments – Removed
Public Housing Capital Fund	Testing of FY 2003 payments in process	Removed – Based on verified corrective actions taken to address the causes of improper payments detected in the testing of FY 2003 payments – Removed
Rental Housing Assistance Programs		
Public Housing	Above Threshold – Based on completed testing of FY 2003 payments	Above Threshold – Based on completed testing of FY 2004 payments
Tenant-based Vouchers & Mod Rehab	Above Threshold – Based on completed testing of FY 2003 payments	Above Threshold – Based on completed testing of FY 2004 payments
Multifamily Project-based Assistance	Above Threshold – Based on completed testing of FY 2003 payments	Above Threshold – Based on completed testing of FY 2004 payments

FHA Payment Systems

FHA's FY 2005 update of their risk assessment of improper payments covered the following 14 activities, which include credit subsidy programs that require special consideration under the Improper Payments Information Act:

- Two payment activities with annual disbursements less than the $40 million threshold;
- Five other payment activities with annual disbursements greater than the $40 million threshold;
- One payment activity on administrative contracts;
- One activity that is for endorsement or loan guarantee commitments; and
- Five activities that are collection systems for FHA.

In the FY 2004 risk assessment of FHA activities, the initial survey determined that only the five payment systems with annual disbursements greater than $40 million warranted a detailed risk assessment. The risk assessment determined that only two of these five areas were at risk for significant improper payments, subject to statistical sampling. Statistical sample testing and evaluation on these two payment systems was completed in FY 2004. Only one of those two systems was found to exceed the improper payment significance threshold in the first year testing to warrant retesting as an at-risk program in FY 2005. No new "at-risk" activities were identified in FHA's FY 2005 risk assessment update. A summary of the FY 2005 payment testing and evaluation update on FHA's one at-risk program follows:

- The Single Family Acquired Asset Management System was subjected to statistical sampling in accordance with OMB guidance. The results indicated a decrease in the improper payment dollar rate from 6.8 percent of total FY 2003 payments to less than 0.6 percent of total FY 2004 payments, with an estimated improper payment dollar amount of $2.2 million in FY 2004. The improvement was attributed to improvements in data identification and collection, as well as increased oversight of the invoice payment process by both staff in the Program Operations Centers and headquarters managers. Since this result was substantially below the $10 million threshold established by the Improper Payments Information Act, this activity has been removed from HUD's inventory of activities at-risk of a significant level of improper payments.

Other HUD Program and Administrative Activities

HUD has 158 distinct funded activities in this category. A total of 127 activities with payments under $40 million were surveyed and determined not to be at risk of improper payments exceeding the $10 million threshold established by the Improper Payments Information Act. These activities constitute $829 million, or less than 2 percent of HUD's total payments in FY 2004.

Detailed risk assessments were conducted on the remaining 31 of HUD's activities with payments over $40 million. The 31 activities covered by the risk assessment constituted $17.8 billion, or 33 percent, of HUD's total FY 2004 payments. Last year, five of those programs, representing $6.1 billion in FY 2003 payments, were determined to be at-risk of a significant improper payment level, pending statistical sample testing. The statistical sample testing of FY 2003 payments in these five identified at-risk program activities was begun during FY 2004 and scheduled for completion in early FY 2005. The reviews were completed, and the HUD independent reviewer determined that only one of these programs, the Public Housing Capital Fund, was susceptible to a significant improper payment level. Corrective actions taken and verified during FY 2005 mitigated the problem in the Public Housing Capital Fund, as discussed below. HUD's FY 2005 risk assessment update in this category fully considered the results of the statistical sampling and corrective actions initiated last year.

Risk assessments of all programs will continue to be conducted and updated on an annual basis, which may result in a change to their assigned risk level.

Public Housing Capital Fund

HUD completed the statistical sample testing for the Public Housing Capital Fund Program and estimated that the total gross improper payments for the program in FY 2003 were $133.5 million or 5.1 percent of the $2.6 billion in total payments covered by the sample testing. The gross improper payment estimate includes $118.1 million in estimated overpayments and $15.4 million in estimated underpayments. The total estimated gross improper payments amount consists of the following two categories of substantive causes of error and two categories of error associated with incomplete sample testing due to time and cost constraints on the testing:

<u>Estimates of Improper Payments Based on Substantive Causes</u>

- $13.9 million estimated for contract retainage amounts that are paid in advance of the need for payment in violation of HUD's cash management policies, and
- $11,000 in estimated other payments without proper supporting documentation.

Estimates of Improper Payments Due to Incomplete Sample Testing

- $96.8 million estimated for payments associated with large, complex monthly funding drawdown/reconciliation processes for which sample testing was not yet completed after allowing six months to provide adequate supporting documentation, and
- $22.7 million estimated for other payments for which sample testing was not completed after HUD's decision to end sample testing after six months because the general level and causes of errors was believed to be known based on completed testing.

Almost all of the improper payment issues discovered during HUD's sample testing related to the largest Capital Fund grant recipient, the New York City Housing Authority, and did not appear to be a program-wide problem. The New York City Housing Authority accounted for 16 of the 211 sampled HUD payment transactions and those 16 large transactions totaled $160.7 million, or 83 percent, of the total sampled dollars of $192.8 million. In response to HUD's review, the New York City Housing Authority changed its contract retention practice and its letter-of-credit drawdown practice to comply with HUD's cash management policies. The Housing Authority also implemented a new financial system in FY 2004 that they claimed eliminated the complex monthly funding drawdown/reconciliation process that hindered the full and timely completion of HUD's sample testing. Based on the results of the testing that was completed, HUD believes that adequate supporting documentation for both categories of incomplete testing items would likely have been provided if additional time had been provided. However, the cost of additional HUD resources to pursue and test those documents outweighed the potential benefit of continuance, given that the causes and corresponding corrective actions for the limited types of errors detected were already known. Under the circumstances, HUD followed up with a review of the New York City Housing Authority's FY 2004-2005 payment transactions under their new practices and financial system, in lieu of another review of payments in the entire Capital Fund Program. The follow-up review conducted in September 2005 verified the corrective actions taken by the Housing Authority to eliminate the causes of the improper payments found in FY 2003. The nature of the improper payment issues originally disclosed in the Capital Fund Program were primarily payment timing issues not subject to recovery actions.

Rental Housing Assistance Programs

HUD's various rental housing assistance programs -- public housing, tenant-based assistance, and project-based assistance -- had previously been assessed as at high risk of significant improper payment levels, and continue to be reported as such, with corresponding error measurement methodologies, corrective action plans, and error reduction goals described below. These programs constituted $26 billion, or 47 percent, of HUD's total payments in FY 2004.

Prior to enactment of the Improper Payments Information Act of 2002, HUD had already established the Rental Housing Integrity Improvement Project in 2001 to reduce improper payments in its rental assistance programs. This project is directed by the responsible HUD program offices, with oversight by the Office of the Chief Financial Officer and statistical sampling support from the Office of Policy Development and Research. HUD's rental assistance programs are administered by over 26,000 public housing agencies and multifamily housing owners or management agents on HUD's behalf. In general, beneficiaries pay 30 percent of their adjusted income as rent, and HUD payments cover the remainder of the rental cost (or the operating cost, in the case of public housing).

There are three major components of potential errors and improper payments in these complex programs:

1) Program administrator error – the program administrator's failure to properly apply income exclusions and deductions and correctly determine income, rent, and subsidy levels;
2) Tenant income reporting error – the tenant beneficiary's failure to properly disclose all income sources and amounts; and
3) Billing error – errors in the billing and payment of subsidies between third party program administrators and HUD.

From FY 2000 through FY 2004, HUD reduced the gross improper payments for the first 2 of these 3 categories of error in its rental assistance programs from $3.2 billion to $1.2 billion, a reduction of 61 percent.

FY 2000 Baseline Error Estimates - A baseline measurement of improper payments due to program administrator error and tenant income reporting was established by two studies completed in FY 2000. The FY 2000 studies verified subsidy calculations and income for a representative sample of 2,403 households receiving assistance at 600 projects. For all 3 major program types, the combined FY 2000 baseline estimates reported for both types of error were $3.281 billion in gross improper payments and $2.013 billion in net subsidy overpayments. The FY 2000 baseline estimates were later adjusted to $3.216 billion in gross improper payments and $1.972 billion in net subsidy overpayments to eliminate the impact of those public housing programs that had been placed under a block grant approach under the Moving To Work Program, which effectively removed them from consideration for error estimates. HUD set goals for reducing the net subsidy overpayments for these two components (i.e., program administrator error and tenant income reporting error) by 15 percent in FY 2003, 30 percent in FY 2004 and 50 percent in FY 2005.

In FY 2005, HUD completed studies of FY 2004 program activity to update the FY 2000 and FY 2003 estimates on the program administrator error and tenant income reporting error components, using the same general methodology, sampling procedures, and sample sizes. The following paragraphs provide details on the FY 2004 rental assistance error measurement updates.

Program Administrator Error - HUD's update of the measure of program administrator rent and subsidy determination errors in FY 2004 found a 55.9 percent reduction in this improper payment component since FY 2000, as shown in the following chart:

Rental Assistance Programs	FY 2004 Full Year Estimates of Error in Program Administrator Income, Rent & Subsidy Determinations				FY 2000 Estimate of Error*	Percent Reduction in Gross Improper Payments
	Assistance Overpayments $1,000's	Assistance Underpayments $1,000's	Net Improper Payments $1,000's	Gross Improper Payments $1,000's	Gross Improper Payments $1,000's	
Public Housing	$173,172	$68,904	$104,268	$242,076	$602,557	*59.8%
Tenant-based Vouchers & Mod Rehab	$366,492	$154,728	$211,764	$521,220	$1,096,535	52.5%
Total PHA Administered	$539,664	$223,632	$316,032	$763,296	$1,699,092	55.1%
Multifamily Project-based Assistance	$141,708	$82,740	$58,968	$224,448	$539,160	58.4%
Total 2004**	$681,372 (+/-$107,203)	$306,372 (+/-$59,293)	$375,000 (+/-$113,149)	$987,744 (+/-$131,201)	$2,238,252 (+/- $271,000)	55.9%

* - Baseline numbers reported in prior years have been reduced to eliminate data associated with PHAs participating in the Moving To Work Program. Those PHAs were excluded from the FY 2004 updated study because they don't follow the same program rules.

** - Estimates are provided at a 95 percent confidence level.

The significant reduction in this error component is attributed to HUD efforts to work with its housing industry partners at PHAs and multifamily housing projects through enhanced program guidance, training, oversight, and enforcement.

Under the Rental Housing Integrity Improvement Project, PIH initiated on-site Rental Integrity Monitoring reviews focused on the 490 largest PHAs that receive 80 percent of HUD's public housing and tenant-based voucher program funds. Technical assistance was provided to PHAs with the most significant program deficiencies and follow-up Rental Integrity Monitoring reviews were conducted to assess program improvements and the need for corrective and enforcement action. The Office of Multifamily Housing has placed nearly all Section 8 Program project-based assistance under Performance-Based Contract Administrators who review 100 percent of monthly vouchers and perform annual on-site management and occupancy reviews at all projects. Twenty percent of the remaining project-based assistance contracts still administered by HUD staff or traditional contract administrators also received on-site monitoring reviews in FY 2004. These same contracts are the subject of an on-going public-private competitive sourcing effort under OMB Circular No. A-76 in an attempt to further improve the monitoring of those contracts.

<u>Tenant Income Reporting Error</u> - HUD estimates that the total error attributable to tenant underreporting of income was $266 million in FY 2004, a decline of 73 percent from the FY 2000 baseline of $978 million. While this is an increase from the FY 2003 estimate of $191 million, this estimate should be regarded as a normal fluctuation as a result of the small sample size and low error rate, rather than an actual increase in error. Program-level estimates are not provided because the low incidence of errors renders any such estimates statistically unreliable.

HUD believes that the general downward trend in tenant income error will continue as the result of an improved methodology for reviewing income discrepancies identified through computer matching to better determine actual cases of underreported income impacting subsidy levels. The reduction will also be facilitated by: improved income verification efforts by housing program administrators; increased voluntary compliance by tenants due to promotion of the issue; and HUD's initiation of improved computer matching processes for upfront verification of tenant income.

In October 2005, HUD's Enterprise Income Verification System will make income data from the National Directory of New Hires available to local PHAs to allow them to conduct more effective and timely income verification for tenants. The National Directory of New Hires, administered by the Department of Health and Human Services, is a central source of all quarterly state wage and unemployment benefit information, as well as monthly employer information on new hires. By the end of FY 2006, HUD plans to consolidate all available income match data sources in the Enterprise Income Verification System for controlled use by program administrators in all HUD rental housing assistance programs, including multifamily housing. This increased computer matching capability has the potential to eliminate the majority of the remaining estimated improper payments attributable to tenant underreporting of income.

Billing Cycle Error – HUD also completed baseline studies for the third and final error component, billing error, in FY 2005. Billing errors occur when program administrators submit billings or payment vouchers to HUD for activities and amounts that: deviate from allowable HUD contract terms and conditions; differ from local rent rolls and subsidy determinations; or pertain to allowable subsidies or utility allowances that are not properly remitted to participating landlords or tenants. In FY 2005, HUD completed baseline measurements for the billing error in the Department's public housing and voucher programs, based on FY 2003 expenditures. The estimated gross billing error was $84 million in public housing and $30 million in the voucher programs (both tenant-based and project-based). Combined with the billing error estimate of $100 million previously established for project-based assistance in FY 2003, HUD's total baseline estimate of improper rental assistance billings is $214 million, as follows:

Results of Billing Error Studies (FY 2003)

Program	Subsidies Overpaid*	Subsidies Underpaid*	Net Billing Error*	Gross Billing Error*
Public Housing	$56	$28	$28	$84
Section 8 Vouchers	$15	$15	$0	$30
Project-based Assistance	$56	$44	$12	$100
Total All Programs	$127	$87	$40	$214

*** Dollars in millions**

Changes to the manner in which the public housing and voucher programs are funded, subsequent to FY 2003, could reduce the opportunity for billing error. In any event, HUD's increased review of payment vouchers and on-site monitoring of support for vouchers is key to reducing this component of improper payments.

Combined Rental Assistance Error Impacts – The combined effect of the most recent accepted estimates of improper payments for the three error components is summarized in the following chart:

Type of Payment Error (Period)	Public Housing Assistance (millions)	Vouchers & Mod Rehab Assistance (millions)	Project-Based Assistance (millions)	Total All Rental Assistance Programs (millions)
Gross Error In Administrator Subsidy Determinations (2004)	$242	$521	$224	$987
Error Due To Tenant Underreporting Of Income (2004) *				$266
Gross Billing Error (2003)	$84	$30	$100	$214
Total Gross Error				$1,467
FY 2004 Program Expense **				$26,069
Percent of Improper Payments				5.6

* - Tenant income error not segmented by program because an accurate estimate was not possible with the associated low error rate.

** - Program expense is shown on an accrual rather than a cash basis to better match the error study methodology.

HUD will continue to take aggressive steps to address the causes of improper rental assistance payments to ensure that the right benefits go to the right people. Based on the above results for the three types of rental assistance error, as well as plans to address known causes and levels of improper payments, HUD provides the statistical results for FY 2004 and the outlook for improper payment percentages on a combined program basis from FY 2005 – FY 2008, as follows:

Rental Assistance Improper Payment Reduction Outlook FY 2004 – FY 2008

(Dollars shown in millions)

Activity	FY 2004 Payments	FY 2004 IP $	FY 2004 IP % Goal/Actual		FY 2005 IP % Goal	FY 2006 IP % Goal	FY 2007 IP % Goal	FY 2008 IP% Goal
Rental Assistance	$26.069	$1.467	6.9	5.6	5.6	5.0	3.0	2.5

Upon completion of the baseline billing error estimates in FY 2005, HUD will break-out separate error reduction goals for each of the three rental assistance program categories. Further information on HUD's efforts to reduce improper rental housing assistance payments is provided in Indicator EM.4.1 in the Performance Information Section of this report.

Recovery Auditing Activity

In addition to the requirements of the Improper Payments Information Act of 2002, Section 831 of the Defense Authorization Act of 2002, and OMB Memorandum No. M-03-07, require agencies that enter into contracts with a total value in excess of $500 million in a fiscal year to carry out a cost-effective program for identifying errors made in paying contractors and for recovering amounts improperly paid to contractors. HUD acquired the services of an outside recovery-audit service provider to assist in: surveying HUD's procurement and contract payment environment for vulnerabilities and opportunities for recovery-auditing; applying recovery-auditing techniques to the universe of HUD contracts completed subsequent to October 1, 2001; and assessing the causes of any recovery opportunities identified, with recommendations for improved controls to avoid improper payments.

The recovery audit service provider found that "the procedures and systems in place at HUD provide strong controls for processing accurate transactions." These identified strengths cited in the final report include the following:

- Procurement and management of contracts provide a high degree of oversight by both HUD and contractor;
- Contract structure limits the risk to transaction error;
- Transaction approval by the HUD Government Technical Representative reduces errors on a per transaction basis;
- System controls applicable to duplicate payments limits the potential of improper payments;
- Established contract "Close Out" procedures to reduce the exposure to outstanding financial items related to the contract; and
- The Ginnie Mae program third party review has proven beneficial to Ginnie Mae in reducing overpayments made to contractors.

The universe of contract activity covered by HUD's recovery auditing project included 568 contracts with a value of $2.27 billion. Sixteen of the larger and more vulnerable contracts with a value of $206.6 million were subjected to a more detailed review. The initial recovery audit results indicated recovery potential of less than $46,000 (0.02 percent). Follow-up by the HUD Contracting Office confirmed that the payments in question were not improper or erroneous.

The recovery audit service provider concluded that, "With respect to the overall volume of contract transactions and dollar amount disbursed by HUD annually, the results of the project indicated the procedures and systems in place at HUD provide strong controls for processing accurate contract payment transactions." Pursuit of an on-going recovery auditing program at HUD was determined not to be cost-beneficial or necessary.

U.S. Department of Housing and Urban Development
Office of Inspector General
451 7th St., S.W.
Washington, D.C. 20410-4500

INDEPENDENT AUDITOR'S REPORT[1]

To the Secretary,
U.S. Department of Housing and Urban Development:

In accordance with the Chief Financial Officers (CFO) Act of 1990, the Department has prepared the accompanying consolidated balance sheets of the Department of Housing and Urban Development (HUD) as of September 30, 2005 and 2004 and the related consolidated statements of net cost, changes in net position, and financing and the combined statement of budgetary resources for the fiscal years then ended. We are required by the Chief Financial Officers Act of 1990, as amended by the Government Management Reform Act of 1994 and implemented by Office of Management and Budget (OMB) Bulletin 01-02, *Audit Requirements for Federal Financial Statements*, to audit HUD's principal financial statements or select an independent auditor to do so. The objective of our audit was to express an opinion on the fair presentation of these principal financial statements. In our previous audit report on the fiscal year 2004 financial statements included in HUD's Fiscal Year 2004 Performance and Accountability Report, we reported that we were unable to complete sufficient audit procedures to express an opinion on the fiscal year 2004 financial statements by the OMB-imposed due date of November 15, 2004. We have subsequently completed that work and we are now able to express an opinion on the fiscal year 2004 financial statements. With respect to the fiscal year 2005 and 2004 financial statements, we did not audit the financial statements of the Federal Housing Administration (FHA) whose statements reflected total assets constituting 34 and 32 percent, respectively, of the related consolidated totals. Other auditors, whose reports have been furnished to us, audited those statements and our opinion on the fiscal year 2005 and 2004 financial statements, insofar as it relates to the amounts included for FHA, is based solely on the reports of the other auditors. In connection with our audit, we also considered HUD's internal control over financial reporting and tested HUD's compliance with certain provisions of applicable laws, regulations, contracts, and grant agreements that could have a direct and material effect on its principal financial statements.

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[1] This report is supplemented by a separate report issued by HUD-OIG to provide a more detailed discussion of the internal control and compliance issues included in this report and to provide specific recommendations to HUD management. The report is available at the HUD, OIG Internet site at http://www.hud.gov/oig/oigindex.html and is titled: "Additional Details to Supplement Our Report on the Audit of the U.S. Department of Housing and Urban Development's Fiscal Years 2005 and 2004 Financial Statements" (2006-FO-0003, dated November 15, 2005) .

Pursuant to the Chief Financial Officers Act of 1990, as amended by the Reports Consolidation Act of 2000 and implemented by OMB Circular Number A-136 *Financial Reporting Requirements*, HUD is required to issue a Performance and Accountability Report that includes, among other information, HUD's annual audited financial statements. For fiscal year 2005, OMB has directed agencies to complete their Performance and Accountability Reports and submit them to the President, OMB and the Congress by November 15, 2005.

Opinion on the Fiscal Year 2005 and 2004 Financial Statements

In our opinion, based on our audit and the reports of other auditors, the accompanying fiscal years 2005 and 2004 principal financial statements present fairly, in all material respects, the financial position of HUD as of September 30, 2005 and 2004 and its net costs, changes in net position, budgetary resources, and reconciliation of net costs to budgetary obligations for the fiscal years then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 2-R to the financial statements, HUD restated its fiscal year 2004 consolidated financial statements to correct accounting errors disclosed during the fiscal year 2005 audit as follows:

HUD restated the balance in Other Intragovernmental Liabilities to Cumulative Results of Operations in accordance with the Statement of Federal Financial Accounting Standards (SFFAS) Number 7, Accounting for Revenue and Other Federal Sources. The balance of $4.2 billion was previously reported as other liabilities in the Department's consolidated balance sheet and represented cumulative activity for the Housing for the Elderly and Disabled Program. The balance sheet reclassification impacted the amount of net position reported for fiscal year 2004 and the components of equity reported on the statement of Changes in Net Position.

In the 2004 Consolidating Statement of Budgetary Resources, the Credit Subsidy Amount transferred by the Government National Mortgage Association (Ginnie Mae) was reported as Spending Authority from Offsetting Collections. The Credit Subsidy amount was reclassified from an offsetting collection to a non-expenditure transfer to comply with OMB Circular A-11 which required that cash transfers to the general fund receipt account be recorded as non-expenditure transfers and should not offset the amount of gross outlays reported on the Statement of Budgetary Resources. These changes resulted in a $405 million adjustment to Ginnie Mae's Net Outlays in the Consolidating Statement of Budgetary

Resources and Resources Used to Finance Activities in the Statement of Financing.

Our audit also disclosed:

- Material weaknesses in internal controls in fiscal year 2005 related to the need to:
  - incorporate better risk factors and monitoring tools into FHA's single family insured mortgage program risk analysis and liability estimation process; and;
  - continue to improve the review over the FHA Credit Reform estimation process.

- Reportable conditions in internal controls in fiscal year 2005 related to the need to:
  - comply with Federal financial management system requirements and continue to enhance FHA's management of controls over its portfolio of integrated insurance and financial systems;
  - improve oversight and monitoring of subsidy calculations and intermediaries' program performance;
  - further strengthen controls over HUD's computing environment;
  - improve personnel security practices for access to the Department's critical financial systems;
  - improve processes for reviewing obligation balances; and
  - improve controls for developing estimates of budget authority required for the Section 236 Interest Reduction Program.

Most of these control weaknesses were reported in prior efforts to audit HUD's financial statements and represent long-standing problems. Our findings also include the following instance of non-compliance with applicable laws, regulations, and provisions of contracts and grant agreements that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 01-02.

- HUD did not substantially comply with the Federal Financial Management Improvement Act. In this regard, HUD's financial management systems did not substantially comply with Federal Financial Management Systems Requirements.

Consolidating Financial Information

We conducted our audit for the purpose of forming an opinion on the consolidated principal financial statements taken as a whole. HUD has presented consolidating balance sheets and related consolidating statements of net costs and changes in net position, and combining statements of budgetary resources and financing as supplementary information in its *Fiscal Year 2005 Performance and Accountability Report.* The consolidating and combining financial information is presented for purposes of additional analysis of the financial statements rather than to present the financial position, changes in net position, budgetary resources, and net costs of HUD's major activities. The consolidating and combining financial information is not a required part of the principal financial statements. The fiscal year 2005 and 2004 financial information has been subjected to the auditing procedures applied to the principal financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

Required Supplementary Information

In its *Fiscal Year 2005 Performance and Accountability Report*, HUD presents "Required Supplemental Stewardship Information," specifically, information on investments in non-Federal physical property and human capital. In addition, HUD presents a Management Discussion and Analysis of Operations and information on intragovernmental balances. This information is not a required part of the basic financial statements but is supplementary information required by the Federal Accounting Standards Advisory Board and OMB Circular Number A-136. We did not audit and do not express an opinion on this information, however, we applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. In accordance with OMB Circular Number A-136, the Department, through confirmations, reconciled their intragovernmental transactions with their trading partners with immaterial differences.

Reportable Conditions:

Additional details on our findings regarding HUD's internal controls are summarized below and were provided in a separate report to HUD management. These additional details also augment the discussions of the instances in which HUD had not complied with applicable laws and regulations; the information regarding our audit objectives, scope, and methodology; and recommendations to HUD management resulting from our audit.

HUD/FHA System Environment Needs to Comply with Federal Financial Management System Requirements. In prior years, OIG reported on weaknesses in HUD's financial management systems, which were described as a material weakness. Specifically, HUD had not completed development of an adequate integrated financial management system. A primary reason was HUD's most significant system deficiency involving FHA. Since 2003, FHA has made progress in correcting the weaknesses in its overall compliance with Federal financial management system requirements through the implementation of the FHA Subsidiary Ledger. A key milestone was achieved during fiscal year 2003 with the implementation of the FHA financial system's general ledger module. In fiscal years 2004 and 2005, FHA completed the implementation of its core financial system implementation with the addition of cash management, funds control, and contract modules. These improvements, combined with progress reported in prior years, enabled OIG to conclude that the remaining issues related to information systems controls no longer constitute a material weakness, and therefore this weakness has been reclassified as a reportable condition.

HUD Management Must Continue to Improve Oversight and Monitoring of Subsidy Calculations and Intermediaries' Program Performance. Since 1996, we reported on weaknesses with the monitoring of housing assistance program delivery and the verification of subsidy payments. Specifically, we focused on the impact these weaknesses had on HUD's ability to (1) ensure intermediaries are correctly calculating housing subsidies and (2) verify tenant income and billings for subsidies. During the past several years, HUD has made progress in correcting this weakness, and in 2005, HUD continued its progress, including taking steps to fully establish a comprehensive program for reducing erroneous payments. These improvements, combined with the progress reported in prior years, enabled OIG to reclassify this weakness as a reportable condition. However, HUD's continued commitment to the implementation of a comprehensive program to reduce erroneous payments will be essential to ensure HUD's intermediaries are properly carrying out their responsibility to administer assisted housing programs according to HUD requirements.

The Department has demonstrated improvements in its internal control structure to address the significant risk that HUD's intermediaries are not properly carrying out their responsibility to administer assisted housing programs according to HUD requirements. HUD's increased and improved monitoring has resulted in a continuing downward trend in improper payment estimates over the last three years. However, HUD needs to continue to place emphasis on its on-site monitoring and technical assistance to ensure acceptable levels of performance and compliance are achieved and periodically assess the accuracy of intermediaries rent determinations, tenant income verifications, and billings.

Controls over HUD's Computing Environment Can Be Further Strengthened. HUD's computing environment, data centers, networks, and servers, provide critical support to all facets of the Department's programs, mortgage insurance, servicing, and administrative operations. In prior years, we reported on various weaknesses with general system controls and controls over certain applications, as well as weak security management. These deficiencies increase risks associated with safeguarding funds, property, and assets from waste, loss, unauthorized use, or misappropriation. We evaluated selected information systems general controls of the Department's computer systems, on which HUD's financial systems reside. Our review found information systems controls weaknesses that could negatively affect the integrity, confidentiality, and availability of computerized data.

Weak Personnel Security Practices Continue to Pose Risks of Unauthorized Access to the Department's Critical Financial Systems. For several years we have reported that HUD's personnel security over critical and sensitive systems' access has been inadequate. Although HUD continues to strive to make progress to address the reported problems, risks of unauthorized access to the Department's critical financial systems remain a major concern. We followed up on previously reported personnel security weaknesses and deficiencies and found that the Department still does not have a central repository that would account for all users with above-read (query) access to all HUD general support and application systems.

HUD Needs to Improve Processes for Reviewing Obligation Balances. HUD needs to improve controls over the monitoring of obligation balances to determine whether they remain needed and legally valid as of the end of the fiscal year. HUD's procedures for identifying and deobligating funds that are no longer needed to meet its obligations are not always effective. This has been a long-standing weakness. Our review of the 2005 year-end obligation balances showed $208 million in excess funds that could be recaptured. Although HUD has made some progress in implementing procedures and improving its information systems to ensure accurate data are used, further improvements in financial systems and controls are still needed.

HUD Needs to Continue Improving Controls for Developing Estimates of Required Budget Authority for the Section 236 Interest Reduction Program. Our review showed an improvement in HUD's procedures and documentation to support the amounts recorded in the subsidiary ledgers. However, we noted that HUD still needs to continue their review of contract files to obtain needed documentation support. There are 51 projects where, due to missing documentation and problems interpreting ambiguous language used in some contracts, HUD could not yet determine if the term of the Interest Reduction Program agreement was 40 or 50 years. To be conservative, HUD assumed that these Interest Reduction Program agreements would be valid for 50 years from the date they were executed. As a result, there is a potential overstatement of the $5 billion cumulative obligation balance ranging from $61 million to $352 million. In addition, we noted four contracts where HUD assumed the agreements were for 50 years and the file documentation supported contract durations of less than 50 years. HUD reduced their obligation balance for the estimated run-out costs for these contracts by $20.6 million.

In addition, our review showed 17 Interest Reduction Program contracts with $148 million in contract and budget authority that could be deobligated. These 17 contracts had either been terminated, prepaid, or the owners had opted-out of the program.

Results of the Audit of FHA's Financial Statements

The independent certified public accounting firm of Urbach, Kahn, and Werlin LLP performed a separate audit of FHA's fiscal year 2005 financial statements. Their report on FHA's financial statements, dated October 28, 2005[2] includes an unqualified opinion on FHA's financial statements, along with discussions of two material weaknesses and one reportable condition. The FHA material weaknesses follow:

> **FHA must incorporate better risk factors and monitoring tools into its single-family insured mortgage program risk analysis and liability estimation process.** Due to significant changes in the home mortgage-lending environment in recent years, the composition and credit worthiness of borrowers in FHA's single family insured loan portfolio has changed, resulting in significant increases in the rate of mortgage insurance claims. However, FHA has not developed a formal process to effectively evaluate certain loan attributes, such as borrower credit scores, down payment assistance sources, delinquency rates and other portfolio characteristics and timely incorporated these factors into the insured loan loss liability calculation to help FHA evaluate the program's future performance.

[2] Urbach, Kahn, and Werlin LLP's report on FHA entitled, "Audit of Federal Housing Administration Financial Statements for Fiscal Year 2005" (2006-FO-0002, dated November 7, 2005) was incorporated into this report.

FHA Management Must Continue to Improve Its Review Over the Credit Reform Estimation Process. Despite continuing improvements to the cash flow models used to estimate the net present value of future premiums, claims and recoveries, and the resulting Loan Guarantee Liability, Urbach, Kahn, and Werlin LLP reported that the management review process over the year end estimate was not sufficient to identify material errors in the Mark-to-Market program and Home Equity Conversion Model (reverse mortgage) cash flow calculations.

The audit results also identified the following reportable condition that is not considered a material weakness:

FHA Must Continue to Enhance the Management of Controls Over Its Portfolio of Integrated Insurance and Financial Systems. As FHA's implementation of its new core financial management system project moves into its final phases, Urbach, Kahn, and Werlin LLP found that the remaining portfolio of various insurance and financial systems that support the financial reporting process are not effectively managed, resulting in continuing general control weaknesses with respect to financial management system's contingency planning, risk assessments, disaster recovery planning, and other components of system security.

Results of the Audit of Ginnie Mae's Financial Statements

We performed a separate audit of the Ginnie Mae financial statements for fiscal years 2005 and 2004. Our report on Ginnie Mae's financial statements, dated November 7, 2005,[3] includes an unqualified opinion on these financial statements. In addition, the audit results indicate that there were no material weaknesses or reportable conditions with Ginnie Mae's internal controls, or material instances of non-compliance with laws and regulations.

For informational purposes, in Note L. to the financial statements, Ginnie Mae makes reference to the Federal Credit Reform Act of 1990, which became effective on October 1, 1991, and notes that in the opinion of

[3] Our report on Ginnie Mae entitled, "Audit of Government National Mortgage Association Financial Statements for Fiscal Years 2005 and 2004" (2006-FO-0001, dated November 7, 2005) was incorporated into this report.

Ginnie Mae management, and HUD's General Counsel, the Federal Credit Reform Act does not apply to Ginnie Mae's guarantee programs. Nevertheless, in consultation with OMB, Ginnie Mae has adopted certain credit reform practices. Because OMB administers the Federal Credit Reform Act and Ginnie Mae's financial position and its net costs, changes in net position, budgetary resources, and reconciliation of net costs to budgetary obligations could be materially impacted by the adoption of all credit reform reporting practices, the Office of Inspector General has requested that OMB's General Counsel formally opine as to whether Ginnie Mae is subject to the full reporting requirements of the Federal Credit Reform Act. In addition, on June 30, 2005, the U. S. House of Representatives passed H.R. 3058, "Making appropriations for the Departments of Transportation, Treasury, and Housing and Urban Development, the Judiciary, District of Columbia, and independent agencies for the fiscal year ending September 30, 2006, and for other purposes." Section 319 of H.R. 3058 states that no funds provided under this title may be used for an audit of Ginnie Mae that makes applicable requirements under the Federal Credit Reform Act of 1990.

Management Deficiencies Represent Long-Standing Weaknesses

Most of the issues described in this report represent long-standing weaknesses that will be difficult to resolve. HUD's management deficiencies have received much attention in recent years. For example, in January 1994, GAO designated HUD as a high-risk area, the first time such a designation was given to a cabinet level agency. Since that time, HUD has devoted considerable attention and priority to addressing the Department's management deficiencies and has made some progress. In their January 2005 update, GAO noted that HUD has made progress since 2003 in addressing identified weaknesses in its high-risk program areas. However, GAO continues to maintain the Department's single-family mortgage insurance and rental housing assistance program areas as high risk at this time.

Because of continued weaknesses in HUD's internal controls and financial management systems, HUD continues to rely on extensive ad hoc analyses and special projects to develop account balances and necessary disclosures.

Objectives, Scope and Methodology

The accompanying principal financial statements are the responsibility of HUD management. Our responsibility is to express an opinion on these principal financial statements. As part of our audit, we considered HUD's internal controls over financial reporting for the purpose of expressing our opinion on the principal financial statements and not to provide assurance on those internal controls. We conducted our audit in accordance with *Government Auditing Standards*, and the requirements of OMB Bulletin 01-02, *Audit Requirements for Federal Financial Statements*, as amended. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion on the financial statements.

We also tested HUD’s compliance with laws, regulations, and provisions of contract and grant agreements that could have a direct and material effect on the financial statements. However, our consideration of HUD’s internal controls and our testing of its compliance with laws, regulations, and provisions of contract and grant agreements were not designed to and did not provide sufficient evidence to express an opinion on such matters and would not necessarily disclose all matters that might be material weaknesses, reportable conditions or noncompliance with laws, regulations, and provisions of contract and grant agreements. Accordingly, we do not express an opinion on HUD’s internal controls or on its compliance with laws, regulations, and provisions of contract and grant agreements.

Agency Comments and Our Evaluation

On October 31, 2005, we provided a draft of the internal control and compliance sections of our report to the CFO and appropriate assistant secretaries and other Departmental officials for review and comment, and requested that the CFO coordinate a Department-wide response. The CFO responded in a memorandum dated November 4, 2005, which is included in its entirety in our separate report. Except for the report’s conclusion on HUD’s compliance with the Federal Financial Management Improvement Act of 1996 (FFMIA), the Department generally agreed with our presentation of findings and recommendations subject to detailed comments included in the memorandum. The Department’s response was considered in preparing the final version of this report.

This report is intended for the information and use of the management of HUD, OMB, the Government Accountability Office, and the U.S.

Congress, and is not intended to be, and should not be, used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited. In addition to a separate report detailing the internal control and compliance issues included in this report and providing specific recommendations to HUD management, we noted other matters involving internal control over financial reporting and its operation that we are reporting to HUD management in a separate "management letter."

James A. Heist
Assistant Inspector General for Audit

November 15, 2005

Management and Performance Challenges ─ Inspector General and HUD Management Perspectives

In accordance with the Reports Consolidation Act of 2000, HUD's annual Performance and Accountability Report "…shall include a statement prepared by the agency's inspector general that summarizes what the inspector general considers to be the most serious management and performance challenges facing the agency and briefly assesses the agency's progress in addressing those challenges." On October 18, 2005, HUD's Inspector General provided a statement on six management challenges for inclusion in this FY 2005 Performance and Accountability Report:

1. Department-wide organizational changes;
2. Financial management systems;
3. Human capital management;
4. FHA single family origination;
5. Public and assisted housing program administration; and
6. Administering programs directed toward the victims of Hurricanes Katrina and Rita.

The full text of the HUD Inspector General's Management and Performance Challenges statement is presented immediately after the following summary of HUD management's current perspective on these challenges.

HUD Management's Perspective

HUD management agrees that the six areas identified in the Inspector General's statement are challenges currently facing the Department. As an indicator of the importance being placed on addressing each of these issues, the first five of these six challenges are included in high-visibility initiatives in the PMA, and the sixth challenge, administering HUD's hurricane disaster relief efforts, is being carried-out in accordance with OMB guidance on expediting benefits and controlling the risk of fraud, waste, and abuse in hurricane disaster relief efforts. In addition to the progress on these challenges that is summarized below, and in the following Inspector General's statement, further information on HUD's specific FY 2005 actions to meet these challenges is provided in the PMA section of this report.

Department-wide Organizational Changes and Human Capital Management – These two challenges are interrelated and are both covered through HUD actions taken and planned under the PMA initiative on "Strategic Management of Human Capital." HUD has taken significant steps to better utilize existing staff capacity, and to obtain, develop, and maintain the capacity necessary to adequately support HUD's future mission-critical program delivery. A five-year strategy for management of human capital has been developed, with detailed implementation plans to ensure that: HUD's organizational structure is optimized; succession strategies are in place to provide a continuously updated talent pool; performance appraisal plans for all managers and staff are linked to HUD's mission goals and objectives; diversity hiring strategies are in place to address under-representation; skill gaps are assessed and addressed; and human capital management accountability systems are in place to support effective management of HUD's human capital. Collectively, these actions are better enabling HUD to recruit, develop, manage, and retain a high-performing workforce that is capable of effectively supporting HUD's program delivery and mission.

Financial Management Systems – FY 2005 was the first time HUD was able to report substantial compliance with the federal financial systems requirements of the Federal Financial Management Improvement Act of 1996 and Section 4 of the Federal Managers' Financial Integrity Act of 1982. HUD's financial systems supported the preparation and audit of Department-wide consolidated financial statements within 45 days after the end of the fiscal year, with an unqualified audit opinion. A full year's operation of new modules of the FHA Subsidiary Ledger Project strengthened support for FHA's cash management, funds control and credit subsidy accounting functions and enabled the Department to eliminate a material weakness issue. With an inventory of 44 total financial systems, the number of non-compliant systems has been reduced from 17 in FY 2003 to only 2 at the end of FY 2005, and remediation of those 2 systems will occur next year. HUD also made significant progress in improving its compliance with systems security documentation and review requirements this past year, to better assure the security of its data. However, since HUD's existing core financial system could be better integrated, more user friendly and less costly to maintain, HUD is proceeding with plans to develop and implement a modern replacement system through the HUD Integrated Financial Management Improvement Project. The requirements for the new system were completed in FY 2005, and HUD is proceeding with plans for development and implementation of the new system by FY 2008.

FHA Single Family Origination – Risks of the FHA Single Family Housing Mortgage Insurance Programs have been reduced through actions taken under the HUD Management and Performance initiative of the PMA, as acknowledged in the Inspector General's statement. Actions taken to date include implementation of: an automated systems control to preclude the predatory lending practice of "property flipping" on FHA insured loans; stronger professional credentials for appraisers who validate the values of FHA insured mortgages; a new "Appraiser Watch" process that automatically targets appraisers with poor performance records for monitoring and disqualification if they have violated FHA standards; a new automated underwriting system to provide more consistent, objective evaluations of the credit worthiness of borrowers; improved risk-based targeting of lender compliance reviews; and a new process for electronic verification of social security numbers to further reduce fraud in FHA applications. With consistent implementation of these and other pending corrective actions initiated by FHA, HUD's goal is to eliminate the Government Accountability Office's high-risk program designation on the Single Family Housing Mortgage Insurance Program area by January 2007.

Public and Assisted Housing Program Administration – HUD set and communicated clear measurable goals and corrective actions for reducing improper rental housing assistance payments and improving public and assisted housing conditions and continues to work collaboratively with the housing industry and local housing program administrators to meet or exceed those goals. Since FY 2000, estimated improper payments due to program administrator subsidy determination errors and tenant underreporting of income have been reduced 61 percent, from $3.2 billion to $1.2 billion. The percentage of properties meeting HUD's physical condition standards has increased to 92 percent for public housing and 96 percent for assisted multifamily housing. HUD's Office of Public and Indian Housing has focused on increased monitoring, technical assistance, and enforcement actions at the largest 490 public housing agencies that receive over 80 percent of their program funding. HUD's Office of Multifamily

Housing and their Performance-Based Contract Administrators conducted over 15,000 on-site monitoring reviews in FY 2005, directed at improving program administrator performance to reduce improper payments and improve housing conditions. The implementation of HUD's new Enterprise Income Verification System for upfront verification of tenant income, in FY 2006, has the potential to eliminate most of the remaining improper payment estimate.

Administering Programs Directed Toward Victims of Hurricanes Katrina and Rita – On August 29, 2005, Hurricane Katrina struck the Gulf Coast, displacing hundreds of thousands of people from their homes. HUD responded quickly in the wake of this unprecedented natural disaster to help meet the temporary housing needs of displaced households, assess the impacts on HUD-supported housing, and plan the long-term recovery of the devastated region. While HUD's response was immediate and comprehensive, it also ensured adequate controls were established over the use of funds to minimize the risk of fraud, waste, and abuse. As an agent of the Federal Emergency Management Agency, the Department has developed and implemented the Katrina Disaster Housing Assistance Payment program to provide temporary housing assistance to all HUD-assisted evacuees as well as those who were homeless prior to the disaster. The controls over this temporary assistance will closely follow HUD's regular housing voucher program to minimize risk of fraud, waste, and abuse. HUD has also approved waivers of many regulations in the Department's programs to ease and expedite access to programs and to provide more flexibility in the use of funds for disaster relief. Again, HUD's normal program oversight will apply to those program activities.

U.S. Department of Housing and Urban Development
Office of Inspector General
451 7th St., S.W.
Washington, D.C. 20410-4500

OCT 18 2005

MEMORANDUM FOR: Alphonso Jackson, Secretary, S

FROM: Kenneth M. Donohue, Inspector General, G

SUBJECT: Management and Performance Challenges

In accordance with Section 3 of the Reports Consolidation Act of 2000, the Office of Inspector General (OIG) is submitting its annual statement to you summarizing our current assessment of the most serious management and performance challenges facing the Department of Housing and Urban Development (HUD) in fiscal year 2006 and beyond. Through our audits and investigations, we work with Departmental managers in recommending actions that best address these challenges. More details on our efforts in relation to these issues can be found in the audit and investigative chapters of our Semiannual Report to the Congress.

The Department's primary mission is to expand housing opportunities for American families seeking to better their quality of life. HUD seeks to accomplish this through a wide variety of housing and community development grant, subsidy, and loan programs. Additionally, HUD assists families in obtaining housing by providing Federal Housing Administration (FHA) mortgage insurance for single-family and multifamily properties. With about 8,800 staff nationwide, HUD relies upon numerous partners for the performance and integrity of a large number of diverse programs. Among these partners are hundreds of cities that manage HUD's Community Development Block Grant funds, hundreds of public housing authorities that manage assisted housing funds, thousands of HUD-approved lenders that originate and service FHA-insured loans, and hundreds of Ginnie Mae mortgage-backed securities issuers that provide mortgage capital.

Achieving HUD's mission continues to be an ambitious challenge for its limited staff, given the agency's diverse mission, the thousands of program intermediaries assisting the Department in this mission, and the millions of beneficiaries in its housing programs. HUD's management problems have for years kept it on the Government Accountability Office's (GAO) list of agencies with high-risk programs. HUD's management team, GAO, and OIG share the view that improvements in human capital, acquisitions, and information systems are essential in removing HUD from its high-risk designation. More specifically, HUD must focus these improvements on rental housing assistance programs and single-family housing mortgage insurance programs, two areas where financial and programmatic exposure is the greatest. That HUD's reported management challenges are included as part of the President's Management Agenda (PMA) is indicative of HUD's important role in the Federal sector. HUD's current Administration places a high priority on correcting those weaknesses that put HUD on GAO's high-risk list.

As of the end of fiscal year 2005, HUD's PMA scoring status showed significant improvement for six of the eight initiatives applicable to HUD with a total of two "green", five "yellow", and one "red" baseline goal scores. Based upon a comprehensive set of standards, an agency is "green" if it meets all of the standards for success, "yellow" if it has achieved some but not all of the criteria, and "red" if it has even one of the number of serious flaws. HUD's baseline score for Improved Financial Performance remains at "red" because of material weaknesses and a disclaimer of opinion received on HUD's 2004 consolidated financial statements. It is noteworthy, however, that HUD was the first agency to receive a "green" baseline goal score on reducing improper payments.

Although the management structure, size, and range of Departmental programs make it difficult to correct and overcome program weaknesses, HUD is working to address these challenges and, as shown by the PMA scoring, has made progress. The Department's management challenges we are reporting this year include:

- ✓Department-wide organizational changes,
- ✓Financial management systems,
- ✓Human capital management,
- ✓FHA single-family origination,
- ✓Public and assisted housing program administration, and
- ✓Administering programs directed toward the victims of Hurricanes Katrina and Rita.

The attachment provides a greater discussion of these challenges and the OIG's efforts to help the Department resolve these matters.

Attachment

Attachment

HUD Management and Performance Challenges

Fiscal Year 2006 and Beyond

***Department-wide Organizational Changes*.** For more than a decade, the Department has struggled with organizational and management changes in an effort to streamline its operations. These changes were necessary as HUD tried to manage more programs and larger budgets with fewer staff. The former HUD Administration realigned the Department along functional lines, separating outreach from program administration. Also, it placed greater reliance on automated tools, processing centers, contracted services, and HUD partners to administer its programs. As HUD implemented these realignments, many employees were assigned new duties and responsibilities, and many new employees were hired. The disruptions caused by these sweeping changes compounded problems in effectively managing HUD operations.

The current Administration has made several changes to reduce organizational layers and improve operations. The Departmental Enforcement Center was placed under the direction of the General Counsel to consolidate legal resources in support of a strong program enforcement effort. The Real Estate Assessment Center (REAC) was placed under the direction of the Assistant Secretary for Public and Indian Housing to improve REAC's working relationships with program staff and program partners. In addition, the return to the former regional and field office structure was implemented to give HUD's field operations greater operational control over the administrative budget resources they need to pursue their operating and program goals and to strengthen the local focus on workload management to meet national performance goals.

Improving the efficiency and effectiveness of HUD's programs through reorganization efforts requires the Department, in part, to sustain operational consistency in completed reforms. To better ensure operational consistency, it is essential that HUD execute its Strategic Five-Year Human Capital Management Plan. The first goal in HUD's Plan, developed in 2003, is to make HUD a mission-focused agency. Getting the right number of employees in the right location with the right skill mix will improve the quality of HUD programs and services by addressing management challenges, reducing program risks, and improving program performance. The relationship between office functions and department wide goals is also reinforced through the Plan's implementation. HUD's Plan recognizes that human resources activities must be aligned with agency goals to clearly, efficiently, and effectively support and enable HUD to achieve its mission.

***Financial Management Systems*.** Since FY 1991, we have annually reported that the lack of an integrated financial system in compliance with all Federal Financial Management System requirements is a weakness in internal controls. While some progress has been made, a number of long-standing deficiencies remain. For the past several years, our financial audits also reported weaknesses in internal controls and security over HUD's general data processing operations and specific applications. The effect of these weaknesses is that HUD cannot be reasonably assured that system information will remain confidential, protected from loss, and available to those who need it without interruption.

HUD has completed certification and accreditation for 41 of its 44 financial management systems. However, the quality of the underlying documents and the actual certification and accreditation process varied by application. While a number of vulnerabilities were closed, additional vulnerabilities, identified through oversight activities, were not corrected before accreditation. In addition, certification and accreditation of the general support systems on which these applications reside has not been completed and is ongoing.

The weaknesses noted in our FY 2004 Consolidated Financial Audit relate to the need to

- Comply with Federal Financial Management System requirements, including the need to enhance FHA's information technology systems to more effectively support its business and budget processes;
- Strengthen controls over HUD's computing environment;
- Improve personnel security practices for access to the Department's critical financial systems; and
- Improve the systems and processes for reviewing obligation balances to ensure that unneeded amounts are deobligated in a timely manner.

HUD's most significant system challenges have existed in FHA, which continues to conduct some day-to-day business operations with legacy-based systems, limiting its ability to integrate its financial processing environment. During FY 2003, FHA implemented the FHA Subsidiary Ledger (FHASL) financial system. This system automated many previously manual processes used to (1) consolidate the accounting data received from the various FHA operational legacy systems and (2) prepare summary entries for posting to the FHASL. FHA continues to make progress in its overall compliance with Federal Financial Management System requirements. In FY 2004, FHA completed the implementation of its core financial system with the addition of cash management, funds control, and contract modules. By FY 2007, FHA plans to fully integrate program operations with its core financial system, eliminating some legacy systems and reengineering others to implement budgetary controls at the source, further reducing the need for manual processing, and improving financial operations.

Human Capital Management. For many years, one of the Department's major challenges has been to effectively manage its limited staff resources to accomplish its primary mission. In recent years, the Department has contracted out numerous functions essential to the accomplishment of its overall mission, in part due to staffing issues. Many of the weaknesses facing HUD, particularly those concerning HUD's oversight of program recipients, are exacerbated by HUD's resource management shortcomings. Accordingly, we consider it critical for the Department to address these shortcomings through the successful completion of ongoing plans. To operate effectively and hold individuals responsible for performance, HUD needs to know that it has the right number of staff with the proper skills in the right positions.

To address its human capital needs and respond to the PMA, HUD developed a comprehensive Five-Year Strategic Human Capital Management Plan that identifies three strategic goals for human capital:

- Mission-focused agency to align employees and work to support HUD's mission;
- High quality workforce, which recruits, develops, manages, and retains a diverse workforce; and
- Effective succession planning to ensure retirees over the next 5 years are succeeded by qualified employees.

The human capital management plan is the Department's primary tool for advancing its human capital transformation. The plan is reviewed annually, and updates or revisions are issued as needed to support implementation activities. In line with its strategic plan, HUD has increased its focus on human capital management through a variety of initiatives.

To address staffing imbalances and other human capital challenges, the Department uses the Resource Estimation and Allocation Process (REAP) and the Total Estimation and Allocation Mechanism (TEAM). REAP and TEAM are HUD's resource management tools by which the Department identifies, justifies, analyzes, and makes a recommendation regarding the optimal level of resources necessary for effective and efficient program administration and management. REAP obtains crucial time and workload data necessary for viable budget estimation and execution and to meet the Department's Government Performance and Results Act requirements.

In June 2003, HUD awarded a contract to conduct a workforce analysis for the Department. The purposes of the workforce analysis studies were to: establish future workforce needs, compare them with current capabilities, determine skill gaps, and develop human capital strategies and actions to close the gaps. In September 2004, the contractor completed the analysis of HUD's workforce and provided HUD a consolidated report with 5-year workforce projections for planning purposes. The contractor's analysis and report focused on the Department's core business functions, beginning with the Office of Public and Indian Housing (PIH), and then the Office of Community Planning and Development, the Office of Housing, and the Office of Fair Housing and Equal Opportunity.

HUD is currently in the process of integrating REAP and the workforce analysis so that they complement one another and provide strategic workforce planning direction with the objective of comparing priority needs and making workforce management decisions that best serve the Department's mission.

FHA Single-Family Origination. FHA's Single Family Insurance Programs enable millions of first-time, minority, low-income elderly and other underserved households to realize the benefits of homeownership. HUD manages about $368 billion in single-family insured mortgages. Effective management of this high-risk portfolio represents a continuing challenge for the Department. The PMA has committed HUD to tackling long-standing management problems that expose FHA homebuyers to fraudulent practices.

HUD has taken a number of actions to reduce risks to homebuyers including the following:

- Established an automated systems control to preclude the predatory lending practice of “property flipping” on FHA insured loans;

- Established an “Appraiser Watch” process, wherein appraisers with poor performance records are automatically targeted for monitoring and disqualification from program participation if they violated FHA standards;

- Established an automated underwriting system, the Technology Open to Approved Lenders (TOTAL) Scorecard to increase lender efficiency through more consistent, objective evaluations of the credit worthiness of borrowers; and

- Initiated a process for the electronic verification of social security numbers to further reduce fraud in FHA applications.

While GAO and we have reported improved monitoring of lender underwriting, default tracking, and expanded loss mitigation to help reduce mortgage foreclosures, HUD needs to further strengthen lender accountability and take strong enforcement actions against program abusers that victimize first-time and minority homebuyers.

In support of HUD and the PMA, OIG’s Strategic Plan for FY 2005 gave priority to detecting and preventing fraud in FHA mortgage lending through targeted audits and investigations. Our audits targeted lenders with high default rates. Our detailed testing focuses on mortgage loans that had defaulted and resulted in FHA insurance losses. Results from these audits have noted significant lender underwriting deficiencies, prohibited late endorsed loans, inadequate quality control, and other operational irregularities. Our recommendations have sought monetary recoveries through loan indemnifications exceeding $197 million, loss reimbursements of over $13.1 million, and appropriate civil remedies. During FY 2005, we completed 50 external audits of FHA-approved mortgage lenders as well as four internal audits of single-family program activities. Additionally, our investigative workload in single-family fraud prevention continues to grow dramatically. Last fiscal year, more than 840 individuals were indicted for single-family fraud.

The OIG’s audit of FHA’s FY 2004 financial statements also reported a need to place more emphasis on monitoring lender underwriting and continuing to improve single-family early warning and loss prevention. OIG has tailored its audit and investigation techniques to complement this need, support HUD management improvements, and provide an added deterrence to mortgage fraud. We developed a comprehensive training course on auditing single-family lenders and conducting single-family fraud investigations. To date, 154 auditors have completed the single-family lender audit training course.

***Public and Assisted Housing Program Administration*.** HUD provides housing assistance funds under various grant and subsidy programs to public housing agencies and multifamily project owners. These intermediaries, in turn, provide housing assistance to benefit primarily low-income households. PIH and the Office of Housing monitor these intermediaries' administration of the assisted housing programs.

Accurate and timely information about households participating in HUD housing programs is necessary to allow HUD to monitor the effectiveness of the program, assess agency compliance with regulations, and analyze the impacts of proposed program changes. The level of reporting is a criterion for housing agencies' performance in both the Public Housing Assessment System and the Section 8 Management Assessment Program. HUD's goal is to obtain 85 percent reporting of tenant data into the system.

Weaknesses in the monitoring of housing agencies and assisted multifamily projects continue to present obstacles in achieving the intended statutory purposes. These weaknesses have been reported for a number of years in our annual audits of HUD's financial statements.

A 2000 HUD study concluded that 60 percent of all rent and subsidy calculations performed by intermediaries contained overpayment or underpayment errors totaling more than $3.2 billion. In 2003, an update to this study estimated a gross error payment of $1.6 billion. Although still a large amount, this represents a 50-percent reduction from the error estimate completed in 2000. The reduction is attributed to enhanced program guidance, training, oversight, and enforcement, as well as improved income verification efforts, voluntary compliance by tenants due to promotion of the issue, an improved computer matching process, and an improved methodology for reviewing income discrepancies. HUD is also validating tenant-reported income against other Federal sources and considering program simplification options. In addition to these efforts, HUD needs to enforce the requirement that intermediaries report data elements in the management information system. Sanctions need to be applied if intermediaries do not comply with this requirement.

Paralleling HUD efforts, our investigative and audit focus is concentrating on fraudulent practices and the lack of compliance with the Section 8 program statute and requirements. To comply with a Congressional request, OIG conducted 35 external audits of the Section 8 Housing Choice Voucher program during FY 2005. The OIG also hired an additional professional appraiser to assist in evaluating housing quality requirements as part of our audit efforts. In total, these external audits addressed whether the housing agencies are correctly calculating subsidy amounts, correctly determining family income, complying with housing quality standards, fully using authorized vouchers, and implementing controls to prevent duplicative and fraudulent housing assistance payments. Our recommendations for these audits questioned costs of over $45.8 million and identified over $194 million that could be put to better use.

Administering Programs Directed Toward Victims of Hurricanes Katrina and Rita. The recent hurricanes devastated many gulf coast communities and displaced millions of people. Initially, the Federal Emergency Management Agency (FEMA) was to be responsible for the temporary housing (up to a year) of evacuees while HUD was to be responsible for finding permanent housing. However, FEMA and HUD later agreed that HUD would receive $79 million to provide transitional housing (up to 18 months) for those individuals who previously received HUD housing assistance prior to being displaced. HUD reports that there are over 700,000 HUD assisted or insured housing units including elderly housing that housed approximately 2 million individuals in the affected region. This new mission of providing transitional and permanent housing for so many displaced people poses significant management and performance challenges for HUD.

HUD has taken a number of actions to address the more immediate housing assistance issues and challenges including:

- Establishing a Hurricane Recovery and Response Center (HRRC), an emergency management division chaired by the Assistant Secretary for Housing-Federal Housing Commissioner that serves as the HUD headquarters command post and reports directly to the Secretary;
- Establishing a field operations office in Baton Rouge, Louisiana and dispatching HUD specialists with expertise on manufactured housing, reconstruction, and community planning;
- Working with the United States Conference of Mayors and the National Association of Counties to coordinate the identification of housing opportunities nationwide;
- Identifying vacant public housing units and available vouchers nationwide;
- Temporarily waiving numerous program requirements to make it easier for disaster displaced individuals who previously received housing assistance to obtain housing assistance in their new locations;
- Modifying or awarding contracts to provide various contractor services to address the housing assistance needs of the displaced hurricane victims; and
- Identifying about 6,000 HUD owned properties within a 500-mile radius of the disaster region and authorizing Management and Marketing contractors to rehab the properties to make them available for housing.

Now that HUD has started the process of providing housing assistance to displaced individuals, it is extremely important that Agency officials work closely with the OIG to ensure that reasonable controls over the use of funds are put in place to mitigate, to the extent possible, the risk of fraud, waste, and abuse. To this end, OIG established a task force to deal exclusively with audit and investigative matters that arise from HUD's disaster recovery and reconstruction responsibilities. It is also important that HUD work closely with FEMA to coordinate the various housing actions undertaken by both Agencies.

Financial Management Accountability

This section covers:

- Federal Managers' Financial Integrity Act Reporting
- Secretary's Audit Resolution Report to Congress
- Delinquent Debt Collection

FMFIA Assurance Statement

I am able to certify with reasonable assurance that the Department is in compliance with the provisions of Section 2 and Section 4 of the Federal Managers' Financial Integrity Act (FMFIA) of 1982. This is the first time HUD has reported an unqualified assurance on compliance with FMFIA, due to the elimination of long-standing material weaknesses on financial systems compliance and controls over rental housing assistance.

Alphonso Jackson
Secretary of Housing and Urban Development

Material Weakness and Systems Non-Conformance

A material weakness is a significant control deficiency that results in more than a remote likelihood that a misstatement significant enough to warrant reporting outside of the agency will not be prevented or detected. Section 2 of FMFIA requires the annual reporting of material internal control weaknesses and plans to correct any such weaknesses. Section 4 of FMFIA requires the reporting of any material non-conformance with financial management systems requirements established by OMB Circular A-127 and the Federal Financial Management Improvement Act of 1996, with corresponding remediation plans.

During FY 2005, HUD continued to focus its efforts on successfully implementing its multi-year corrective action strategies to address the remaining material internal control weakness and long-standing material systems non-conformance. FY 2005 marked a milestone for the Department, as both of HUD's two remaining material weakness issues were reduced to reportable conditions, as discussed below.

Material Weakness
FY 2004 Carry Over Issue and FY 2005 Status

First Reported	Material Weakness	Status at End of FY 2005
1996	Controls Over Rental Housing Assistance[4]	Reportable Condition

Remaining Material Weakness Reclassified as Reportable Condition

The Department's comprehensive strategy for addressing weaknesses in its internal controls over subsidy determinations and payments in its rental housing assistance programs progressed to the point where the material weakness has been reclassified as a reportable condition. These programs, which include Public Housing, Section 8 Tenant-Based Assistance, and Multifamily Housing Project-Based Assistance, were collectively designated as a "high risk" program area by the Government Accountability Office, pending their next updated review in January 2007. HUD's Office of Inspector General also reported material internal control weaknesses in this area prior to reclassifying the material weakness as a reportable condition in their FY 2005 financial statement audit. HUD has made substantial reductions in erroneous housing subsidy determinations and payments through enhanced program guidance, training, oversight, and enforcement. Upon full implementation of a new computer matching system for upfront verification of tenant income in FY 2006, HUD expects to resolve the remaining reportable condition issue and justify elimination of the high-risk program designation for rental housing assistance. Additional information on completed and planned corrective actions on this weakness is provided in the President's Management Agenda section of this report, under the initiative to eliminate improper payments.

Material Non-Conformance
FY 2004 Carry Over Issue and FY 2005 Status

First Reported	Material Non-Conformances	Status at End of FY 2005
1989	Departmental Financial Management Systems	Reportable Condition[5]

Material Systems Non-Conformance Reclassified as Reportable Condition

As a result of continued progress made in the area of HUD's financial management systems, this long-standing material non-conformance has been downgraded to a reportable condition, and HUD is now substantially compliant with OMB Circular A-127 and the Federal Financial Management Improvement Act of 1996. Compliance with OMB Circular A-127 is assured when the system meets all of the 12 requirements contained in Section 7 of the Circular. If the system does not comply with one or more factors, the impact of the non-conformance instance is assessed against the overall ability of the system to generate reliable financial information

[4] This material weakness was presented in 1999 and prior reports as "Income Verification." In FY 2000, HUD expanded the weakness to include all issues associated with improving controls over rental subsidies, including a previously reported management concern entitled "Project-Based Subsidy Payments."

[5] The FHA Accounting and Management Systems material non-conformance, previously shown separately, was combined as a part of the Departmental Financial Management Systems non-conformance in FY 2003.

consistently, accurately, and uniformly. OMB guidelines specify that agencies are substantially compliant with the Federal Financial Management Improvement Act if they can:

- Prepare financial statements and other required financial and budget reports using information generated by the financial management system(s);
- Provide reliable and timely financial information for managing current operations;
- Account for their assets reliably, so that they can be properly protected from loss, misappropriation, or destruction; and
- Do all of the above in a way that is consistent with federal accounting standards and the Standard General Ledger.

HUD's core financial management systems were deemed to be substantially compliant with the Federal Financial Management Improvement Act in FY 2001, with the exception of FHA systems where there was a need to convert from a commercial accounting system to a system that complied with federal requirements, including accounting for budget execution and funds control and credit reform. FHA designed and initiated the multi-year, phased FHA Subsidiary Ledger Project to better address FHA's business needs and comply with federal financial management systems requirements. The general ledger module of the FHA Subsidiary Ledger system was implemented in October 2002, to provide the capability to: record and track budgetary resources using the U.S. Standard General Ledger at the transaction level; control expenditures against available resources (on a monthly basis); and produce timely financial statement reports directly from the general ledger. In late FY 2004, FHA implemented the accounts payable, accounts receivable, procurement, and projects modules of the project to strengthen support for cash management, funds control, and credit subsidy accounting. The project has now moved into the final phase of completing the improved integration of insurance program operations with the new core financial system. In addition, this phase will include strengthening the FHA Subsidiary Ledger System's disaster recovery planning, risk assessment, and contingency planning process, and other components of system security.

A complete listing of HUD's 44 financial and mixed financial program systems is shown in Appendix 3. Of these 44 financial management systems, only 2 are reported as non-compliant: the Facilities Integrated Resources Management System in the Office of Administration, and the Loan Accounting System in the Office of the CFO. This is a significant improvement given the 17 non-compliant systems reported at the beginning of FY 2003.

In FY 2005, an independent contractor determined that the Facilities Integrated Resources Management System was not in compliance with FMFIA due to significant internal control weaknesses. In its 2005 FMFIA assurance statement, the Office of Administration reported the Facilities Integrated Resources Management System as non-compliant with Section 4 of FMFIA. The Office of Administration, while having compensating controls to periodically reconcile the property inventory maintained in the Facilities Integrated Resources Management System with the various purchasing activities, also has corrective actions in process to address systemic internal control deficiencies to better ensure that the system maintains a current, accurate, and complete property inventory.

The Office of the CFO is in the process of replacing the Loan Accounting System, which accounts for the terminated direct loan program for the Section 202 program (elderly housing). The Office of the CFO awarded a contract for procuring a commercial-off-the-shelf package for the Loan Accounting System in March 2005 and purchased the software in April 2005. The system configuration and testing of the software started in May 2005 and continued through the fourth quarter of FY 2005. The implementation of the commercial-off-the-shelf replacement system is projected to occur during the second quarter of FY 2006.

Reportable Conditions

To be consistent with terminology used in the revised OMB Circular A-123, weaknesses previously reported as management concerns are now shown as reportable conditions. Reportable conditions are control deficiencies that represent weaknesses in the design or operation of internal control that could adversely affect the organization's ability to meet its internal control objectives. HUD began FY 2005 with 9 reportable conditions and ended the fiscal year with 10 open conditions, having combined 2 issues, opened 1 new issue and downgraded 2 issues from material weaknesses to reportable conditions, as discussed above. The table following this summary chart provides specific FY 2005 accomplishments and remaining actions on each of the other reportable conditions.

Reportable Conditions
FY 2004 Carry Over Issues and FY 2005 Status

Carry Over/New Issues	Reportable Conditions	Status at End of FY 2005
RC1	Performance Measures*	Open
RC3	PHA Monitoring	Open
RC4	HUD's Computing Environment*	Open
RC5	Personnel Security Over Systems*	Combined with RC4
RC7	Obligation Balances*	Open
RC12	FHA Systems Controls	Combined with RC19
RC13	Resource Management	Open
RC14	Management Controls	Open
RC16	Single Audit Act Coverage	Open
RC17	FHA Risk Analysis/Liability Estimation**	New
RC18	Controls Over Rental Housing Assistance*	Downgraded from a MW
RC19	Departmental Financial Management Systems*	Downgraded from a MW

**Reportable Conditions in the Office of Inspector General's FY 2005 Financial Statement Audit*

***Material Weakness in the Office of Inspector General's FY 2005 Financial Statement Audit*

Status of Reportable Conditions

Reportable Condition/ Problem Statement	FY 2005 Accomplishments	Planned Actions
Performance Measures HUD needs to improve quality controls over performance measure data to ensure data: 1) accuracy, 2) timeliness, 3) estimation, and 4) availability.	• Completed five additional data quality assessments and certifications of HUD information systems used to support Annual Performance Plan reporting. HUD concluded the data quality improvement process on 28 total systems.	• Implement all corrective actions identified during data quality assessments. • Complete certification of systems not yet certified. • Assess and address data availability and quality issues associated with the accelerated Performance and Accountability Report.
PHA Monitoring Continued efforts are needed to improve monitoring of PHAs to ensure that program funds are expended in compliance with laws and regulations.	• Assessed monitoring management and operations of 11 field offices during the Quality Management Review on-site visits and provided technical assistance, as appropriate. • PIH participated in the Department's Compliance and Monitoring Initiative Training for FY 2005. The three-day training consisted of a general session to train staff on the commonalities of monitoring, as well as program-specific training. A total of 34 PIH staff were trained.	• Implement plans to annually conduct comprehensive monitoring reviews on 100 of the 480 largest PHAs and on a 5 percent sample of the remaining PHAs. • Improve the consistency and tracking of the reporting and resolution of monitoring results. • Continue the Quality Management Review on-site visits. • Continue delivery of the Compliance and Monitoring Initiative to field office staff.
HUD's Computing Environment Controls over HUD's computing environment can be further strengthened to reduce the risks associated with safeguarding funds, property, and assets from unauthorized use or misappropriation.	• Developed HUD's security Certification and Accreditation program. • Completed Certification and Accreditation for more than 90 percent of all of HUD's systems. • Completed contingency plan for 41 HUD mission critical systems in accordance with National Institute of Standards and Technology 800-34 publication. • Completed the implementation of the new Microsoft Windows XP operating system for all employees' desktop personal computers. • Standardized Microsoft Windows XP configuration to the National Institute of Standards and Technology standards where practical. • Oversaw the HUD Information Technology Service contract under which the following was carried out: determination and/or revision of any contingency requirements; compliance with the continuity of operations plan; and compliance with the National	• Monitor agency progress on Plan of Action and Milestones in accordance with the Federal Information Security Management Act. • Revise and update the Security and Privacy Architecture for the Target Enterprise Architecture. • Complete, implement, and test a disaster recovery plan for HUD's information technology infrastructure. • Implement a compliance review process to ensure conformance with published security baseline configuration standards. • Complete the contingency plan for each major HUD application, in accordance with the National Institute of Standards and Technology 800-34 publication. • Implement Alpha-Five, the replacement system for the HUD

Reportable Condition/ Problem Statement	FY 2005 Accomplishments	Planned Actions
	Institute of Standards and Technology guidelines.	On-Line User Registration System, which was to provide administrative workflow, multilevel approvals, self-registration, and reporting, but is no longer supported for upgrade.
Personnel Security HUD's personnel security practices need to be strengthened to reduce the risks of unauthorized access to the Department's critical financial systems.	• Performed 100 percent of the FY 2005 reviews, by comparing access security data with data residing in the personnel security's database.	The remaining action on this reportable condition was combined with the above reportable condition on HUD's Computing Environment, pending completion of Alpha-Five.
Obligation Balances HUD needs to improve controls over the monitoring of obligated balances to determine whether they remain needed and legally valid as of the end of the fiscal year.	• Changes to Section 8 funding processes and recapture policies and procedures were completed to address prior OIG audit concerns on large obligation balances on expired contracts. • Performed a 100 percent reconciliation and reconstruction of records for the Section 236 Interest Reduction Program to establish a revised remaining obligation balance of $5 billion, and provided for an improved integration and automation of the business and accounting processes to maintain accurate program balances going forward.	• Fully implement the new Section 236 accounting process. • Resolve the 51 Section 236 projects with missing documentation or ambiguous contract terms. • Strengthen controls over obligation balances on the Office of Housing's project-based assistance programs.
FHA Systems Controls Continued improvement is needed in the area of ADP application security, system support, and preparation and maintenance of system documentation.	• Completed the Certification and Accreditation of all major FHA information technology applications in accordance with National Institute of Standards and Technology guidelines. • Included Underwriting Reporting System functionality into the Computerized Home Underwriting Management System and the FHA Connection system. • Completed Multifamily Housing blueprint. • Completed Project Mobilization and Business Diagnosis phases for Rental Housing Assistance Business Process Reengineering. • Completed define phase of Loan Origination Module, the first module for Single Family Integration.	This reportable condition was combined with the reportable condition on HUD's Departmental Financial Management Systems, discussed earlier in the report.

Reportable Condition/ Problem Statement	FY 2005 Accomplishments	Planned Actions
Resource Management HUD needs to develop a comprehensive strategy to manage its resources and better estimate staffing needs and support its staffing requests.	• Established an executive team to develop a vision of the future HUD workforce, including a multi-year implementation plan. • Issued a Departmental Workforce Implementation and Action Plan that identified crosscutting issues in the four core business areas and included a comprehensive listing of actions and milestones to address staffing and skill gap issues. • Aligned the performance plans of all employees with the Department's strategic goals. • Launched the HUD Integrated Human Resource and Training System, a comprehensive web-based system that automates and re-engineers the Human Resources processes, thus improving the speed and accuracy of critical human resource transactions. • Established Workforce Analysis Planning Committees for HUD's core business programs and began implementing short- and long-term strategies by utilizing the Departmental Workforce Implementation and Action Plan. • Issued a Departmental Succession Planning Strategy that links to the Departmental Workforce Plan and Strategic Human Capital Management Plan. Guidance supports the identification of leadership talent pools with skills assessments to confirm gaps and subsequent training plans to close those gaps. • Reduced the hiring timeline for non-Senior Executive Service positions in accordance with the Office of Personnel Management's approved model. • Issued new guidance to streamline the Senior Executive Service hiring timeline.	• Measure the closure of competency gaps for Leadership Pool employees and current managers and supervisors. • Develop a revised Salaries and Expenses budget request to address skill gaps identified in workforce plans. • Conduct an accountability review with Office of Personnel Management participation; examine results; and develop strategies to strengthen human capital accountability. • Reduce the Senior Executive Service hiring timeline by 58 percent. • Complete workforce analyses and plans for the remaining HUD program and support offices.
Management Controls Weaknesses in the Department's control environment impact its ability to effectively manage its programs.	• Continued participation in the Quality Management Review Program, evaluating field office performance to identify deficiencies and develop corrective solutions. Eleven reviews were completed in FY 2005.	• Update the Departmental Management Control Handbook 1840.1 Rev-3 to reflect OMB Circular A-123 changes that became effective October 2005. (continued)

Reportable Condition/ Problem Statement	FY 2005 Accomplishments	Planned Actions
	• Revised the HUD Monitoring Desk Guide and provided Compliance and Monitoring Training to monitoring staff on assessment of program effectiveness. • Completed risk assessments to identify program control risks and develop monitoring strategies. • Awarded a contract to assist with implementation of the new OMB Circular A-123, Appendix A requirements.	• Continue to mitigate control weaknesses and other deficiencies. • Issue A-123 assurance statement on controls over financial reporting.
Single Audit Act Coverage HUD needs to improve its oversight of program participant compliance with the Single Audit Act requirements and consider central oversight of single audit results.	• Awarded a contract to develop a centralized Single Audit Act system that assists in the Department's Single Audit Act responsibilities. • Sustained testing during HUD's Quality Management Reviews to determine the adequacy of single audit follow-up by field office staff. • Issued instructions to Office of Community Planning and Development field staff on Single Audit Act requirements. • Drafted Department-wide policy for the Single Audit Act requirements. • Expanded use of the Image Management System.	• Continue system design and development of a central Single Audit Act tracking system. • Implement Departmental policy and guidance on the processing and use of single audits.
FHA Risk Analysis/Liability Estimation FHA must improve its use of risk factors and monitoring tools to better predict and limit liabilities.	• Reclassification from a material weakness in FY 2005. • Implemented a new underwriting review process that focuses on risk to the FHA insurance fund. Loans are rated as acceptable or unacceptable for credit and property underwriting. • Continued to improve the use of the Technology Open To All Lenders Scorecard to evaluate risk of individual loans. • Continued to improve cash flow models used to estimate Loan Guarantee Liability. Data validation process was developed to compare actual to projected data.	• Develop a formal process to evaluate the impact of individual loan factors, including borrower credit scores and downpayment assistance sources on the FHA portfolio. • Expand the validation process developed in FY 2005 to compare the prior year's projected and actual cash flows to develop HUD's independent expectations for gross cash flows and other key ratios.

Secretary's Audit Resolution Report to Congress

This information on the Department of Housing and Urban Development's audit resolution and follow-up activity covers the period October 1, 2004, through September 30, 2005. It is required by Section 106 of the Inspector General Act Amendments (Public Law 100-504), and provides information on the status of audit recommendations without management decisions and recommendations with management decisions, but no final action. The report also furnishes statistics on the total number of audit reports and dollar value of disallowed costs for FY 2005, and statistics on the total number of audit reports and dollar value of recommendations that funds be put to better use.

Audit Resolution Highlights

During FY 2005, the Department achieved 790 approved management decisions and successfully implemented 749 recommendations. The Department also made good progress in reducing its rolling inventory of overdue final actions. HUD began the year with 163 recommendations with overdue final actions and ended the year with 53, for a net reduction of 110 overdue recommendations. This was a result of a deliberate and concerted Department-wide effort to strongly address overdue recommendations.

On September 16, 2005, a Hurricane Katrina Audit Resolution Working Group was formed by the Department and directed to consider the impact of Hurricane Katrina on audit resolution. The Group identified 8 audits and 57 recommendations that were significantly affected. To provide program action officials ample time to consider Hurricane Katrina's impact on existing recommendations, the working group extended the final action target dates for the 57 recommendations to April 15, 2006. Action officials will use this time to reassess pre-Katrina action plans to see if they still make sense. Appropriate actions may include timely completion of previously planned actions, ratification of existing action plans with new final action target dates, fully revised action plans, or requests for closure of recommendations that are no longer applicable, to include the write-off of debt.

These hurricane-impacted recommendations were flagged in the Audit Resolution Corrective Action Tracking System, and progress toward removing each "flag" will be encouraged and monitored by the Working Group. The Department also authorized the working group to designate additional recommendations as disaster-impacted, as may become necessary due to additional hurricanes or other future disaster-related events.

Recommendations Without Management Decisions

The Department is statutorily required to provide a management decision (an action plan with milestones) for each audit recommendation within 6 months of report issuance by the Inspector General.

FY 2005 began with a total of 255 recommendations without a management decision. During the year, 806 recommendations requiring management decisions were added to our active workload, and timely management decisions were made on a total of 790 recommendations. FY 2005 ended with 271 recommendations without management decisions, with just four beyond the statutory period of six months. Following the close of the year, the Inspector General approved management decisions for these four recommendations.

Summary of Recommendations Without Management Decisions
October 1, 2004 - September 30, 2005

Opening Inventory	255
New Audit Recommendations Requiring Decision	806
Management Decisions Made	(790)
Audit Recommendations Awaiting Management Decisions	271
Audit Recommendations Beyond Statutory Period	4

Recommendations With Management Decision But No Final Action Taken

The Department began the year with an inventory of 872 management decisions requiring final action. During the year, 790 additional management decisions were made, the Department completed final action on a total of 749 recommendations, and one additional audit recommendation was reopened. The total number of audit recommendations with management decisions but final actions not yet completed at the end of the year was 914. Of this 914, 50 are under active multi-year repayment plans that will remain open until the collection activities are completed.

At the beginning of FY 2005, the Department established an annual performance goal for each program office within HUD to reduce the opening balance of final actions that were more than 12 months overdue by 50 percent. At the beginning of FY 2005, there were 33 final actions that were more than 12 months overdue. During FY 2005, 95 recommendations could have become more than 12 months overdue for a total of 128 recommendations in that category. However, 93 of the 128 recommendations were closed during FY 2005, leaving a balance of 35 final actions that were more than 12 months overdue at the end of FY 2005. While the Department did not meet its goal of halving the number of these significantly overdue recommendations, all program offices, save one, ended the year with zero recommendations overdue by 12 months or more. In addition, the Department reduced its total inventory of overdue recommendations from a beginning balance of 163 overdue recommendations to 53 overdue recommendations at year's end. This 67 percent reduction is an exceptional improvement.

Summary of Recommendations With Management Decisions And No Final Action October 1, 2004 - September 30, 2005

Opening Inventory	872
Management Decisions Made During FY 2004	790
Sub-Total No Final Action at End of Period	1,662
Final Action Taken	(749)
Audit Recommendations Reopened During Period (Without Final Action)	1
Total Audit Recommendations Requiring Final Actions	914[1]

[1] *The Department has 50 recommendations under current repayment plans. These recommendations are considered open and count in the audit inventory until final repayment is made.*

Status of Audits With Disallowed Costs

As of October 1, 2004, there were 155 audits with management decisions on which final action had not been taken, with a dollar value of disallowed costs totaling $246 million. During FY 2005, management decisions were made for 87 audits with disallowed costs totaling approximately $162.4 million. The Department had 62 audits in which final action was taken during the fiscal year, with approximately $23.8 million in recoveries and $35.8 million in write-offs. As of September 30, 2005, there were 180 audit reports with recommendations involving disallowed costs awaiting final action, with an associated value of approximately $348 million.

Note that the Inspector General Act requires reporting at the audit report level versus the individual recommendation level. At the audit report level, total disallowed costs in the report are reported as open until all recommendations in a report are closed. When reporting is done at the more detailed recommendation level, the $348 million of disallowed costs awaiting final action are reduced by $90 million (see the notation below corresponding to footnote 4).

Management Report on Final Actions on Audits With Disallowed Costs
For the Fiscal Year Ended 9/30/05

Classification	Number of Audit Reports	Disallowed Costs
A. Audit reports with management decisions on which final action had not been taken at the beginning of the period.	155	$245,603,741
B. Audit reports on which management decisions were made during the period.	87	$162,404,892
C. Total audit reports pending final action during period.	242	$408,008,633
D. Audit reports on which final action was taken during the period.		
1. Recoveries	51[1]	$23,805,539
(a) Collections and offsets	45	$22,126,360
(b) Property	0	0
(c) Other	9	$1,679,179
2. Write-offs	37	$35,862,497
3. Total of 1 and 2	62[2]	$59,668,036
E. Audit reports needing final action at the end of the period (subtract D3 from C)	180[3]	$348,340,597
	(346)[4]	($259,881,899)

[1] *Audit reports are duplicated in D.1.(a) and D.1.(c), thus the total is reduced by 3.*

[2] *Audit reports are duplicated in both D.1 and D.2; thus the total is reduced by 26.*

[3] *Litigation, legislation, or investigation is pending for 24 audit reports with costs totaling $102,941,278.*

[4] *The figures in brackets represent data at the recommendation level as compared to the report level.*

Status of Audits With Recommendations That Funds Be Put to Better Use

At the beginning of FY 2005, there were 47 audits with management decisions on which final action had not been taken with recommendations to put funds to better use (i.e., used more efficiently), with a dollar value of approximately $3.5 billion. During FY 2005, management decisions were made for 73 audits with funds put to better use costs totaling approximately $1.5 billion. The Department had 27 recommendations for which final action was taken during the fiscal year with a dollar value of $132.9 million, and seven recommendations totaling $10.1 million that management concluded should not or could not be implemented. At the end of the year, there were 92 audits with recommendations to put funds to better use awaiting final action with an associated value of approximately $4.8 billion.

Note that the Inspector General Act requires reporting at the audit report level versus the individual recommendation level. At the audit report level, total funds put to better use in the report are reported as open until all recommendations in a report are closed. When reporting is done at the more detailed recommendation level, the $4.8 billion of funds put to better use costs awaiting final action is reduced by $3.4 billion (see the notation below corresponding to footnote 3).

Management Report on Final Action On Audits With Recommendations That Funds Be Put to Better Use For The Fiscal Year Ended 9/30/05

Classification	Number of Audit Reports	Disallowed Costs
A. Audit reports with management decisions on which final action had not been taken at the beginning of the period.	47	$3,522,698,401
B. Audit reports on which management decisions were made during the period.	73	$1,452,250,953
C. Total audit reports pending final action during period (Total of A and B).	120	$4,974,949,354
D. Audit reports on which final action was taken during the period		
1. Value of recommendations implemented (completed)	27	$132,965,094
2. Value of recommendations that management concluded should not or could not be implemented	7	$10,103,156
3. Total of 1 and 2	28[1]	$143,068,250
E. Audit reports needing final action at the end of the period (Subtract D3 from C).	92[2]	$4,831,881,104
	(85)[3]	($1,455,927,593)

[1] Audit reports are duplicated in D.1. and D.2, thus the total is reduced by 6.

[2] Litigation, legislation, or investigation is pending for 9 audit reports with costs totaling $248,882,873.

[3] The figures in brackets represent data at the recommendation level as compared to the report level.

Delinquent Debt Collection

Fiscal Year Ending	Total Debt (In millions)	Delinquent Debt (In millions)	Delinquent Debt Collections (In millions)
2005*	$12,686	$730	$550

*The above totals reflect FY 2005 data from the Third Quarter Treasury Report on Receivables Due from the Public. The Treasury Report on Receivables for the Fourth Quarter was not available in time for incorporation into this report. The vast majority of these totals are comprised of debts from FHA and Housing programs. Less than one percent of delinquent debt originates from all other HUD programs. The Housing Financial Operations Center in Albany, New York, administers the vast majority of delinquent, eligible debts that HUD refers to the Department of the Treasury.

HUD's Financial Operations Center remains committed to maximizing collections on delinquent debts using all available collection tools. The Albany staff continues to work closely with systems contractors and the Department of the Treasury to achieve the systems and process improvements necessary to maintain compliance with the Debt Collection Improvement Act.

During FY 2005, HUD submitted 18,677 delinquent debtors to Treasury's National Delinquent Debtor Database for potential offset via the Treasury Offset Program. This program is a centralized offset program, administered by Treasury's Financial Management Service, to collect delinquent debts owed to federal agencies and states in accordance with federal law. Offset collections during FY 2005 totaled $12.7 million for the Department. HUD also referred 1,953 new debts to Treasury for cross-servicing during the year, which totaled $10.8 million. Cross-servicing is the process whereby federal agencies refer delinquent debts to Treasury for collection. The Debt Collection Improvement Act of 1996 designates Treasury for collecting these debts on a government-wide basis.

The Department also mailed 2,769 "Notice of Intent" letters to delinquent debtors advising them that their debts were past due. These notices provide debtors with the right to establish repayment plans or appeal the enforceability of debts through the HUD Board of Contract Appeals or, for federal employees, through an Administrative Law Judge. Debtors who fail to make payment arrangements or exercise their appeal rights are referred to Treasury, where they are subjected to aggressive collection efforts, including offset of federal payments, referral to private collection agencies, and administrative wage garnishment.

During March 2005, HUD obtained access to the U.S. Court Systems' Public Access to Court Electronic Records. This system offers inexpensive, fast, and comprehensive bankruptcy case information on active and recently closed cases, and has allowed HUD to operate more efficiently handling accounts where the debtor(s) is involved in bankruptcy.

In September 2005, HUD responded to the Hurricane Katrina disaster by suspending all active collections against debtors located within the FEMA-designated disaster areas. The Department will re-evaluate the situation in early 2006 to determine the next appropriate actions with respect to the affected debtors.

Among federal agencies, HUD continued to spearhead use of Administrative Wage Garnishment via the Treasury Cross Servicing Program. Treasury reported $1.7 million in these collections for HUD debt during FY 2005, with 388 active Wage Garnishment Orders in place at the end of the fiscal year. To take full advantage of this collection tool, the Department is currently developing an internal administrative wage garnishment program that will target eligible debtors that may have been through the Treasury collection process prior to Treasury's implementation of this collection tool. HUD fully expects that this new program will result in increased collections.

The Department continues to use the Electronic On-line Solutions for Complete and Accurate Reporting to respond electronically to consumer disputes that are filed regarding HUD's credit reporting of delinquent debts. The Consumer Data Industry Association makes this system available to consumer reporting agencies, mortgage reporting companies, and data furnishers to facilitate the resolution of disputes as required by the Fair Credit Reporting Act. During FY 2005, HUD responded to 1,600 credit reporting disputes using this system, and also continued its efforts to convert to the new industry standard, the Metro 2 credit-reporting format.

To ensure the Financial Operations Center remains current on debt collection methods, the Albany staff obtained training from the Department of Treasury Financial Management Services staff in June 2005 on Treasury's comprehensive new debt collection system, FedDebt. This online financial system manages debts referred to Treasury by federal agencies in accordance with the Debt Collection Improvement Act. FedDebt is an interactive system and it is expected to become operational in December 2005. As a result of the training, HUD staff are now prepared to interact effectively with FedDebt.

HUD's Financial Operations Center remains committed to using all available tools to maximize the return on its debt collection efforts, thereby returning the greatest possible value for each taxpayer dollar.