THE MISSION OF HUD

The first FHA Insured Home

INCREASE HOMEOWNERSHIP, SUPPORT COMMUNITY DEVELOPMENT, AND INCREASE ACCESS TO AFFORDABLE HOUSING FREE FROM DISCRIMINATION.

These words, from HUD's Strategic Plan, go back to the heart of the United States Housing Act of 1937 which declared it a national policy to "assist the several states and their political subdivisions to remedy the unsafe and unsanitary housing conditions and the acute shortage of decent, safe, and sanitary dwellings for families of lower income and … to vest in local public housing agencies the maximum amount of responsibility in the administration of their housing programs."

Subsequent legislative and political changes have broadened the scope of the nation's housing policy, and in 1965 the United States Congress established the Department of Housing and Urban Development (HUD) as an Executive, Cabinet-level agency, to:

- Foster the orderly growth and development of the nation's urban areas,
- Coordinate Federal activities affecting housing and urban development,
- Provide technical assistance and information to aid state, county, town, or other local governments in developing solutions to community and metropolitan development problems,

- Encourage effective regional cooperation in the planning and conduct of community and metropolitan development programs and projects,
- Encourage and develop the fullest cooperation with private enterprise in achieving the objectives of the Department, and
- Conduct continuing comprehensive studies, and make available findings, with respect to the problems of housing and urban development.

HUD's Strategic Plan and Performance Goals

HUD's strategic planning process provides a framework for effective planning, budgeting, program evaluation, and accountability for results. The result of this process is this annual report to the President, Congress, and the public.

HUD's four-tiered performance management framework to measure performance begins by setting strategic goals and is illustrated in the following chart:

DESCRIPTION	
Strategic Goals	HUD has three programmatic Strategic Goals and three cross-cutting goals directed toward meeting its mission.
Strategic Objectives	Broad operational focus areas designed to achieve Strategic Goals. HUD has 16 programmatic strategic objectives and 11 cross-cutting objectives.
Performance Indicators	Specific measurable values or characteristics used to measure progress towards achievement of strategic objectives. HUD uses four different types of indicators: outcome, output, milestone, and percentage (benchmark). Additionally, tracking measures are used to report valuable data where there are substantial limits on HUD's span of control.
Performance Targets	Quantifiable expressions of desired performance/success levels.

HUD's Strategic Framework

HUD's mission statement and the six Strategic Goals shown in the following chart are integral parts of the Department's planning process reflecting and helping to ensure the continuity of HUD's policies and operations. Three of the strategic goals are programmatic goals that address the specific, but separate, complimentary mission goals of HUD: to promote homeownership, provide decent affordable rental housing, and strengthen our communities. Three other Strategic Goals are cross-cutting goals that support each of the first three. A companion discussion that summarizes the public benefit and resources HUD uses to achieve its mission through key program and policy activities, measurements, and results is found in Section 2, Performance Indicators. The table on the following page provides a depiction of HUD's Strategic Goals and the objectives of each.

HUD'S STRATEGIC FRAMEWORK

MISSION: INCREASE HOMEOWNERSHIP, SUPPORT COMMUNITY DEVELOPMENT, AND INCREASE ACCESS TO AFFORDABLE HOUSING FREE FROM DISCRIMINATION.

Programmatic Strategic Goals

A: Increase homeownership opportunities

- A1: Expand national homeownership opportunities.
- A2: Increase minority homeownership.
- A3: Make the homebuying process less complicated and less expensive.
- A4: Reduce predatory lending through reform, education, and enforcement.
- A5: Help HUD-assisted renters become homeowners.
- A6: Keep existing homeowners from losing their homes.

B: Promote decent affordable housing

- B1: Expand access to and availability of decent, affordable rental housing.
- B2: Improve the management accountability and physical quality of public and assisted housing.
- B3: Improve housing opportunities for the elderly and persons with disabilities.
- B4: Promote housing self-sufficiency.
- B5: Facilitate more effective delivery of affordable housing by reforming public housing and the Housing Choice Voucher program.

C: Strengthen communities

- C1: Assist disaster recovery in the Gulf Coast region.
- C2: Enhance sustainability of communities by expanding economic opportunities.
- C3: Foster a suitable living environment in communities by improving physical conditions and quality of life.
- C4: End chronic homelessness and move homeless families and individuals to permanent housing.
- C5: Address housing conditions that threaten health.

Cross-Cutting Strategic Goals

D: Ensure equal opportunity in housing

- D1: Ensure access to a fair and effective administrative process to investigate and resolve complaints of discrimination.
- D2: Improve public awareness of rights and responsibilities under fair housing laws.
- D3: Improve housing accessibility for persons with disabilities.
- D4: Ensure that HUD-funded entities comply with fair housing and other civil rights laws.

E: Embrace high standards of ethics, management, and accountability

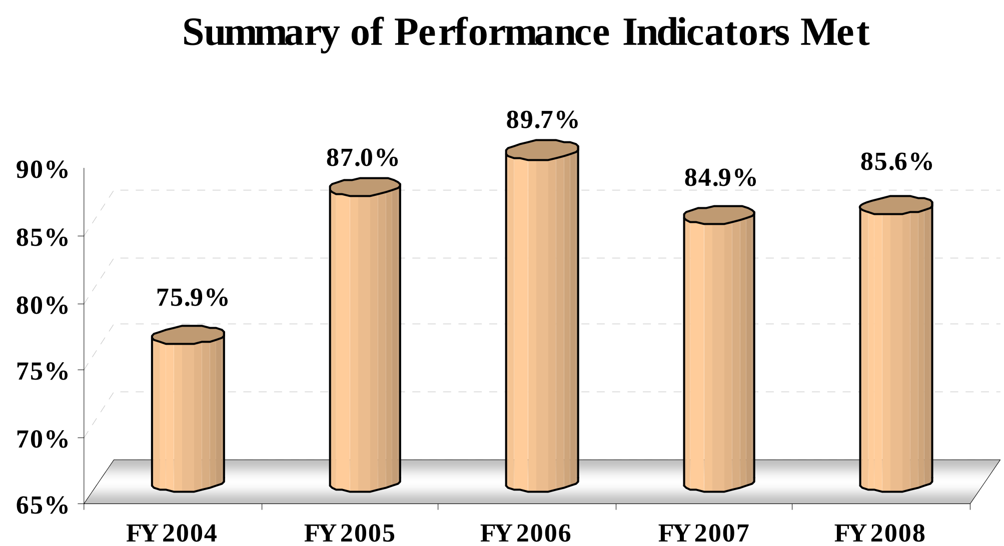
- E1: Strategically manage HUD's human capital to increase employee satisfaction and improve HUD performance.
- E2: Improve HUD's management and internal controls to ensure program compliance and resolve audit issues.
- E3: Improve accountability, service delivery, and customer service of HUD and its partners.
- E4: Capitalize on modernized technology to improve the delivery of HUD's core business functions.

F: Promote participation of faith-based and community organizations

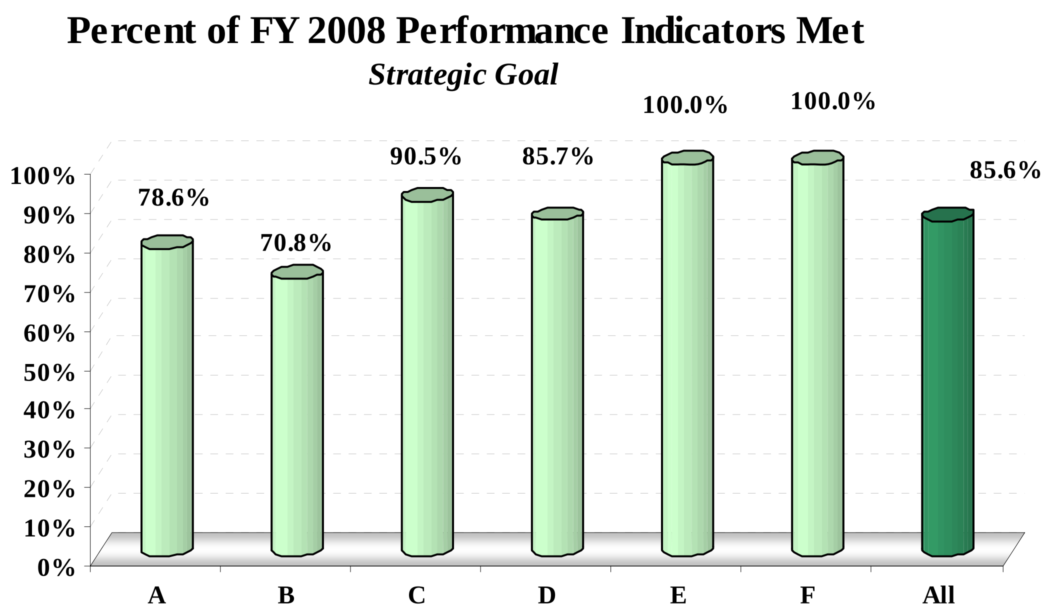
- F1: Reduce barriers to faith-based and community organizations' participation in HUD-sponsored programs.
- F2: Conduct outreach and provide technical assistance to strengthen the capacity of faith-based and community organizations to attract partners and secure resources.
- F3: Encourage partnerships between faith-based/community organizations and HUD grantees and sub-grantees.

Performance Overview

The Department is required to report on its actual performance related to the performance indicators and targets published in the Department's FY 2008 Annual Performance Plan. Below is a graphical summary of our performance on all indicators over the past five years, FY 2008 indicators by Strategic Goal, and FY indicators by Program Office.



Fiscal Year 2008 performance reflects a slight increase over FY 2007 results, though it is still below the levels established in FY 2005 and FY 2006. The Department's ability to achieve a higher success rate was hindered by the downturn in the economy as it has affected the housing industry (see the section entitled Risks, Trends, and Factors Affecting Goals contained in this section of this report), as well as from a relative reduction in funding available for HUD program monitoring, assistance, enforcement, and for needed IT systems improvement. For a broader explanation of HUD's means, strategies, and plans for accomplishing its Strategic Goals, see the introduction to Section 2, the Performance Section. The details regarding each performance indicator, including a description of the public benefit, background, and current results, can also be found in Section 2.



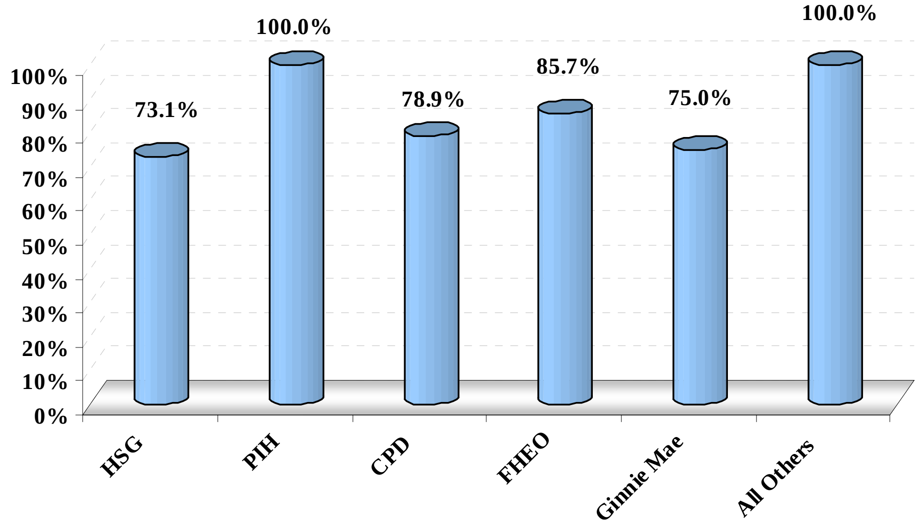
A: Increase Homeownership Opportunities; **B:** Promote Decent Affordable Housing; **C:** Strengthen Communities
D: Ensure Equal Opportunity In Housing: **E:** Embrace High Standards of Ethics, Management and Accountability;
F: Promote Participation of Faith-Based and Community Organizations

In order to most efficiently and effectively fulfill the Mission of HUD, the Department has established the following program offices:

- Office of Housing (including the Federal Housing Administration),
- Public and Indian Housing (PIH),
- Community Planning and Development (CPD), and
- Office of Fair Housing and Equal Opportunity (FHEO).
- Government National Mortgage Association (Ginnie Mae),

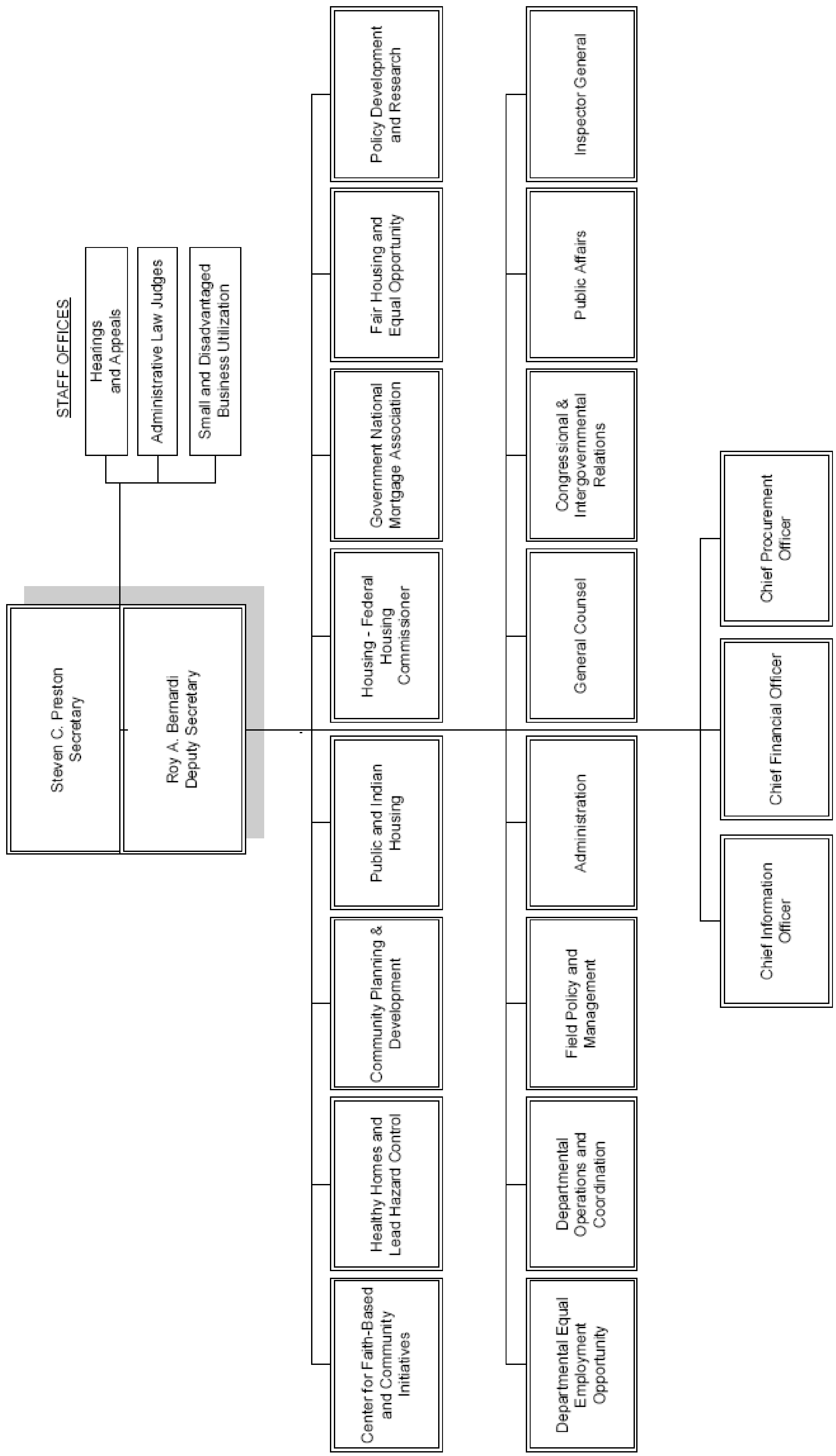
Each office has a primary focus on one or more of the Strategic Goals of HUD's Mission, and their programs are generally focused on a particular housing program delivery constituency, such as state and local governments (CPD), public housing agencies (PIH), private sector lenders and owners (Housing/FHA), or the secondary mortgage market (Ginnie Mae). Additionally, HUD has a number of other administrative, financial, and support offices that directly support the Mission goals and/or provide valuable support to the five major program offices.

Percent of FY 2008 Performance Indicators Met
Program Office



The following pages provide a snapshot of the Department's major organizations and their respective programs, how they work and who they serve and their accomplishments and challenges during FY 2008. Additionally, in the following section are other program and support organizations that address a specific housing area and/or perform a specific function. Each office's specific performance measures are discussed in depth in the Performance Section (Section 2) of this report. Section 2 details the FY 2008 results, explaining HUD's successes and challenges, and how HUD addressed the challenges.

DEPARTMENT OVERVIEW

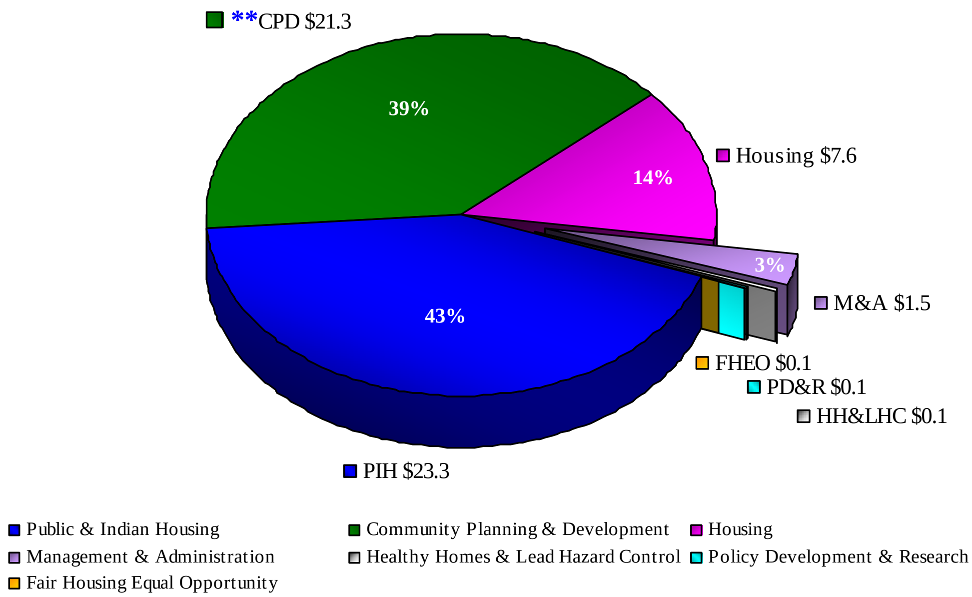


September 30, 2008

HUD PROGRAM OFFICES

The following chart illustrates the new discretionary Budget Authority provided to HUD by the Congress in FY 2008. In addition, HUD has permanent indefinite authority for some of its FHA and Ginnie Mae program activity, based on revenues generated by those self-sustaining programs over the years. The chart does not reflect rescissions of prior year funds. Salaries and Expenses (S&E) in the amount of $1.2 billion, including expenses for Information Technology of $234 million, are reflected in Management and Administration (M&A). Ginnie Mae is not reflected in the chart because it receives only S&E appropriations ($8.3 million) that are included in M&A.

HUD FY 2008 Discretionary Gross Budget Authority (*$54.0 billion)
Dollars In Billions



**Gross budget authority does not include the enacted $1.3 billion overall rescission directed to be from any available HUD resources, and does not include the $723 million enacted rescission directed from the Section 8 Tenant Based Rental program, or $37.6 million directed from the Section 236 Rental Assistance Program (RAP).*

***CPD budget includes $13.7 billion in supplemental funding for disaster recovery and associated foreclosure assistance, which occurred in FY 2008.*

OFFICE OF HOUSING

Primary Focus: Increase Homeownership Opportunities and Affordable Rental Housing

Major Programs: FHA Single Family and Multifamily Housing Mortgage Insurance, Section 8 Project-Based Rental Assistance, Section 202 Housing for the Elderly, Section 811 Housing for the Disabled, Housing Counseling

FY 2008 Budget Authority
Gross Appropriated Budget Authority: $7.6 Billion
Insurance and Loan Guarantees: $181+ Billion
FHA Collections: $15.7 Billion
Authorized Staffing: 3,108 Full Time Equivalent

Performance Indicators
Number of Measures: 26 Number Met: 19 Number Missed: 7

Program Web Address: http://www.hud.gov/offices/hsg/index.cfm

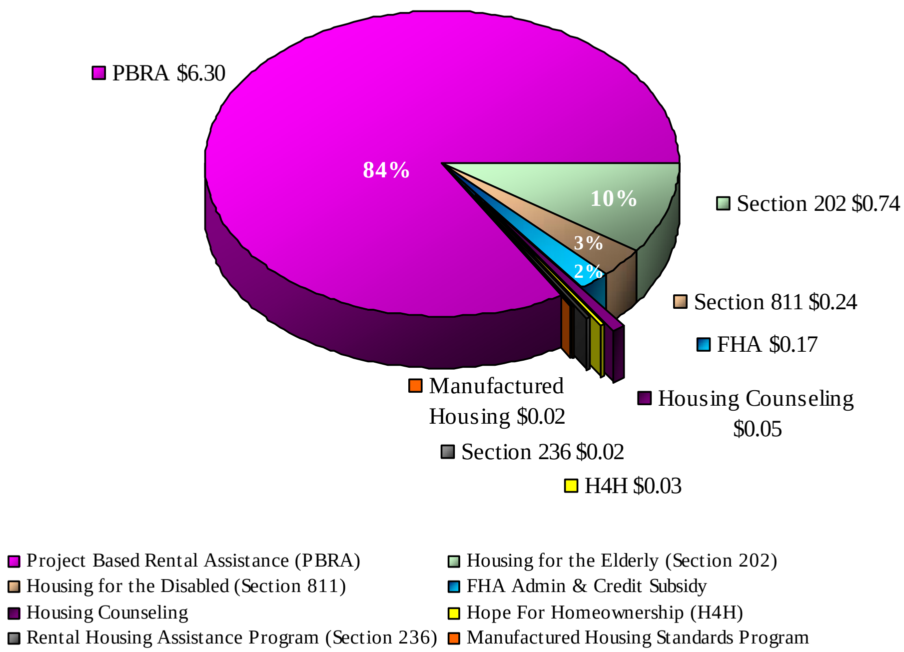
The Office of Housing consists of the Federal Housing Administration (FHA), a government corporation within HUD, and various other programs that support a mission to contribute to building and preserving healthy neighborhoods and communities; to maintain and expand homeownership, rental housing and healthcare opportunities; and to stabilize credit markets in times of disruption. The three business areas that support the mission of the Office of Housing are Single Family Housing, Multifamily Housing, and Regulatory Programs.

These Housing programs provide mortgage insurance on loans for the purchase of new or existing homes, condominiums, manufactured housing, and houses needing rehabilitation; facilitate the construction, substantial rehabilitation, refinancing, and purchase of multifamily housing projects and healthcare facilities; and provide elderly homeowners with reverse equity mortgages. Within the Office of Housing, the Office of Regulatory Affairs and Manufactured Housing also regulates and enforces the Real Estate Settlement Procedures Act to protect homebuyers; regulates interstate land sales to protect consumers from fraud and abuse; regulates construction and enforces construction standards for certain factory built housing units, known as manufactured homes; and establishes minimum property standards for buildings constructed under HUD housing programs.

The Office of Housing is partially funded through Congressional appropriations, which totaled $7.6 billion in FY 2008. The FHA insurance program is primarily funded through insurance premiums collected from borrowers when they obtain an FHA insured mortgage. The credit subsidy, which is the present value of the estimated difference between the long term cost to the government (for defaults, delinquencies, and other payments for FHA insured loans) and the amount collected (from fees, premiums, penalties, and recoveries), is also funded through the appropriation process.

The following chart displays the major components of the Office of Housing's FY 2008 Gross Budget Authority.

HOUSING
Gross Budget Authority FY 2008 ($7.6 billion)
Dollars In Billions



FHA's Mission and History

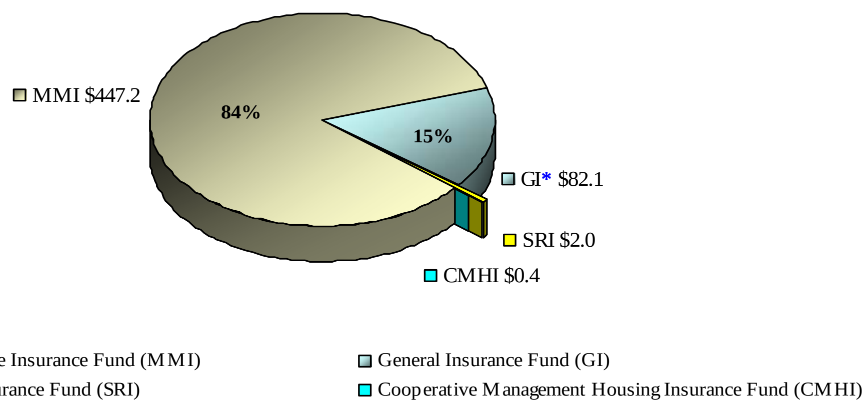
The FHA was established in 1934 with the primary purpose of increasing homeownership at a time when two million construction workers had lost their jobs, mortgage terms were limited to 50 percent of a home's market value, and only four in 10 households owned homes. In that environment, FHA began insuring home mortgages, allowing lenders to provide upfront versus annual market rate loans to all eligible purchasers. When a borrower obtains an FHA insured mortgage, he or she pays an upfront premium and an annual premium to FHA. The proceeds from those premiums are used to fund FHA program costs, including claims on defaulted mortgages and (with disposition of properties conveyed to HUD through foreclosures on FHA insured mortgages) holding costs, property management fees, property sales, and other associated costs.

FHA has been, and continues to be, a stabilizing presence for credit markets in times of economic disruption, as it did when private insurers tightened standards and some closed their businesses during the deep regional recessions of the 1980s. In the current credit crisis, FHA is providing a financially conservative and stabilizing presence, as will be discussed below.

Over the past 74 years, FHA has provided insurance for over 35 million home mortgages (contributing to a current homeownership rate of over 68.1 percent) and for over 50 thousand multifamily project mortgages. FHA's current portfolio contains approximately 4.5 million insured single family mortgages and 12 thousand insured multifamily projects (containing 1.4 million household units). In the last two years, these single family numbers have begun to expand dramatically, primarily due to the many subprime mortgages which are being refinanced through FHA.

FHA programs operate through four insurance funds supported by premium and fee income, interest income, Congressional appropriations, borrowing from the Treasury, and other miscellaneous sources. By collecting mortgage insurance premiums and other fees, most FHA programs are self-sustaining. The four funds are the Mutual Mortgage Insurance (MMI) Fund, the General Insurance (GI) Fund, the Special Risk Insurance (SRI) Fund, and the Cooperative Management Housing Insurance (CMHI) Fund. MMI, which supports FHA's basic single family homeownership programs, is the most prominent fund and is self-sustaining with its unpaid principal balance representing 84 percent of the total insurance-in-force.

FHA Insurance In Force ($531.7 billion)
Dollars In Billions



* *HECM are not included in the amount for GI Insurance-In-Force due to the unique nature of the program. As of September 30, 2008, the maximum potential liability for HECM's was $78 billion.*

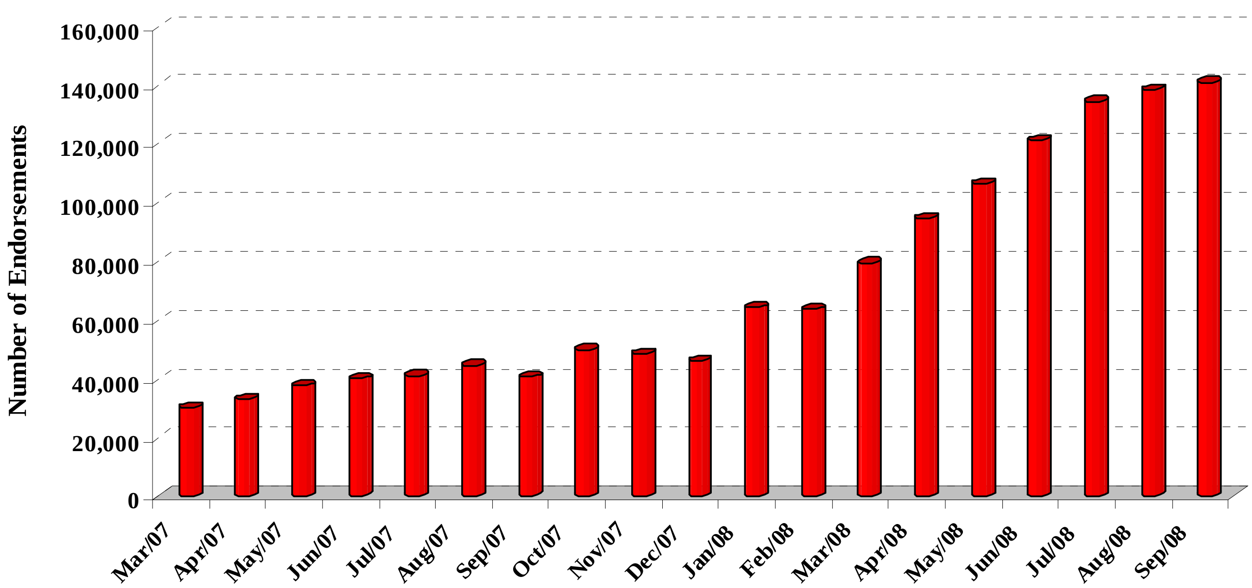
- *The Mutual Mortgage Insurance (MMI) Fund.* This fund supports FHA's basic single family homeownership programs. This fund is self-sustaining.
- *The General Insurance (GI) Fund.* This fund receives direct appropriation and supports a wide variety of housing programs including rental apartments, cooperatives, condominiums, nursing homes, hospitals, property improvements, manufactured housing (Title I), home equity conversion mortgages, and disaster assistance.
- *The Special Risk Insurance (SRI) Fund.* This fund receives direct appropriation and supports higher-risk single family and multifamily insured mortgages.
- *The Cooperative Management Housing Insurance (CMHI) Fund.* This fund supports insured loans on market-rate cooperatives. Historically, this fund has been self-sustaining.

Additional information about FHA can be found in its annual report available on the web at: http://www.hud.gov/offices/hsg/fhafy08annualmanagementreport.pdf.

FHA's role in improving homeownership opportunities is tracked by the volume of FHA insured loans. (For more detailed information, see Section 2, Performance Section, Indicators A.1, A.2, A.5, and A.6.) During FY 2008, FHA endorsed new mortgage insurance for over 1.2 million single family mortgages including 111,661 Home Equity Conversion Mortgages (HECM), representing $177 billion of new mortgage endorsements. This is up from over 532 thousand endorsements in FY 2007 representing $60 billion of mortgage insurance coverage. Of the new endorsements in FY 2008, 77.9 percent were to first time homebuyers, with 31.2 percent being made to minorities.

In 2002, the President announced the Minority Homeownership Initiative to add 5.5 million minority homeowners by the end of the decade (i.e., between the second quarter of 2002 and the last quarter of 2010). By the end of the third quarter of 2008, 4.992 million minority homeowners have been added, accomplishing 91 percent of the goal, with only 74 percent of the time having elapsed.

Recent FHA Endorsement Trends
March 2007 - September 2008



As of the end of the fiscal year, there were 4,377,795 outstanding single family home mortgages insured by FHA, representing an outstanding unpaid principal balance of $475 billion.

The *Home Equity Conversion Mortgage* program enables elderly homeowners to access the equity in their homes and continue to occupy their homes with no repayment requirement until the property is vacated or sold. In FY 2008, 111,661 endorsements were for reverse mortgages, having a maximum potential liability of $24 billion.

The financial stability of the Mutual Mortgage Insurance fund is a major concern of HUD and the Congress. To ensure the stability of this fund, Congress has mandated a minimum level for the capital ratio, currently set at 2.0 percent. The capital ratio is defined as the ratio of estimated economic value of the Fund to outstanding insurance-in-force. Economic value is a measure of the excess of resources available to FHA over its liabilities. Resources include assets plus the present value of expected future premium revenues on outstanding loan guarantees. Liabilities are the (present value of) expected future claim payments on outstanding loan guarantees. Economic value, the difference between these two, is then a cushion against adverse and unexpected changes in future loan performance. The capital ratio has consistently exceeded this minimum requirement, and was 6.4 percent in FY 2007. In FY 2008, HUD again surpassed the minimum level, though this ratio decreased significantly to 3.0 percent. This decrease was caused by two primary factors. The estimated economic value of the fund decreased significantly with the forecast of expected house price declines due to the declining housing market. Conversely, the total MMI insurance in force increased significantly due to the volume of new endorsements. The combination of these factors resulted in the decrease in the capital ratio. Directly related to the decrease in the capital ratio, FHA projected a significant increase in its Liability for Loan Guarantees. This projected additional liability is recorded to reflect anticipated future losses as a result of increased claim rates and reduced recovery rates.
Much of the increased activity in the FHA single family programs during FY 2008 is due to the decrease in interest rates and the increase in FHA mortgage refinancing due to the crisis in the subprime mortgage lending and the reset of Adjustable Rage Mortgages (ARMs). Additionally, higher FHA loan limits, decreasing home prices, and tightening of available credit have encouraged low- and moderate-income buyers to seek out traditional financing available through FHA Insurance Programs that offer buyers flexible down payment options. For an in depth explanation of HUD's response to the resulting financial crisis, see the report on "Risks, Trends, and Factors Affecting Goals," found elsewhere in this section.

FHA's multifamily programs provide mortgage insurance to HUD approved lenders to facilitate the construction, substantial rehabilitation, purchase and refinancing of multifamily housing projects and healthcare facilities. The loans are for all facility types (apartments, co-ops, nursing homes, assisted living, and mobile home parks) except for hospitals and medical group practices. Because FHA insurance and Risk Sharing guarantees protect lenders if borrowers default, these tools make lenders more willing to finance multifamily housing and contribute directly to HUD's strategic goal of providing decent and affordable housing. This year, the FHA endorsed mortgage insurance for 647 new multifamily housing loans (representing 70,914 units) and 8 new healthcare facilities, bringing the totals to 11,931 multifamily housing loans and 81 healthcare facilities, and representing an aggregate of $4.17 billion of insurance coverage. (For more detailed information, see Section 2, Performance Section, indicator B.4.) Although the number of multifamily endorsements fell short of the FY 2008 goal, the results still represent a significant achievement in light of the major economic downturn impacting our country.

Rental Housing

The Office of Housing administers rental subsidy, homeownership subsidy, and grant programs designed to provide housing to low- and moderate-income persons. HUD seeks to increase the number of available affordable rental housing units through insuring loans for multifamily projects or providing subsidies on existing projects. The latter is provided via three legislative provisions: Section 8 Project-Based Rental Assistance; Section 202 Supportive Housing for the Elderly; and Section 811 Supportive Housing for Persons with Disabilities.

Section 8 Project-Based Rental Assistance

The Section 8 Project-based Rental Assistance Program, named for the section of the U.S. Housing Act of 1937 under which the original subsidy program was authorized, differs from the Housing Choice Voucher program (described in the Public and Indian Housing section of this report) in that the assistance is not provided to individual families, but is instead attached to multifamily housing properties to ensure that these properties remain affordable to low income families. In FY 2008, approximately 1.3 million units were provided Section 8 assistance.

Section 202 Supportive Housing for the Elderly

Established by a provision of the Housing Act of 1959, Section 202 authorizes HUD to provide interest free capital advances to private, non-profit sponsors to finance the development of supportive housing for the elderly. The advance need not be repaid as long as the project serves very low-income elderly persons, including the frail elderly, for at least 40 years. Rent subsidies are also provided in order to make the facilities affordable. (For more detailed information, see Section 2, Performance Section, Indicators B.11, B.12, B.13, and B.14.)

The Grand Opening of Glengarra Place in Missoula, Montana, took place on February 20, 2008. The 41-unit development, funded under HUD's Supportive Housing for the Elderly Program, was developed by the KillKenny Corporation with support from the Missoula Housing Authority and the City of Missoula, Montana. HUD's contribution was $4,719,029 for project construction, plus rental assistance to cover the difference between HUD-approved operating costs and the tenants' contribution. The development serves very low-income seniors.

Section 811 Supportive Housing for Persons with Disabilities

Authorized by the National Affordable Housing Act of 1990, the Section 811 subsidy operates in a similar manner as Section 202. Section 811 provides affordable housing for very low-income households in which at least one member, 18 years or older, has a physical or developmental disability or chronic mental illness. (For more detailed information, see Section 2, Performance Section, Indicators B.11, B.13, and B.14.)

The goals for Section 202 and Section 811 were combined in FY 2008. The target was to reach initial closing on 200 projects. The actual number closed was 224 projects, which resulted in an additional 4,560 Section 202 units and 1,137 Section 811 units.

Physical Condition Standards

Ensuring the quality and viability of subsidized housing also is a major commitment of the Department, and HUD has established a goal to monitor the physical and financial condition of insured and assisted multifamily housing projects.

The Office of Insured Housing enforces the physical standards established by HUD which are applicable to multifamily Section 8, Section 202, and Section 811 dwellings that provide housing for families. As of the end of FY 2008, 93 percent of 31,497 properties met physical condition standards as reported in the Physical Assessment Subsystem. This result failed to meet the FY 2008 target by 2 percent. (For more detailed information, see Indicator B.9.) Given the level of funds, and an aging housing stock, it has been difficult to meet the standards. However, HUD will continue to look to provide adequate resources not only to maintain, but improve the physical condition of the housing stock.

Finally, the Department strives to ensure that multifamily projects are managed well financially. HUD monitors multifamily project owners for compliance with HUD established financial management standards, and, through its Financial Assessment Subsystem, identifies financial risks and compliance deficiencies that need loss mitigation or enforcement action. The percentage of multifamily project owners found to be compliant with HUD financial management standards in FY 2008 was 99.9 percent, surpassing the goal of 98 percent. (For more information, see Indicator B.10.)

Regulatory Programs

The Office of Housing also operates programs for overseeing regulations that protect homeowners and homebuyers. Among these is the administration of the Real Estate Settlement Procedures Act (RESPA). The RESPA is a consumer protection statute enforced by HUD. This Act helps consumers be better shoppers in the home buying and mortgage loan process by requiring that consumers receive disclosures at various times in the transactions and by prohibiting practices, such as paying kickbacks, that increase the cost of settlement services. The Act also provides consumers with protections relating to the servicing of their loans, including proper escrow account management. For more information, go to http://www.hud.gov/respa. HUD's FY 2008 goal was to respond to 3,000 inquiries and complaints related to RESPA. HUD responded to 5,578 inquiries, far exceeding its goal. In March of 2008, HUD proposed a rule to revise RESPA, which will be published in the first quarter of FY 2009, in order to simplify and improve the process of obtaining mortgages and reduce consumer settlement costs. Once made final, this rule will help consumers make better informed decisions concerning the various provisions of their loan documents, especially with regard to interest resets and early payment penalties.

FHA Reform

As a result of the housing crisis, there was an extraordinary amount of legislation passed in FY 2008. The following is a brief description of that activity.

The sharp increase in mortgage foreclosures experienced during FY 2008 occurred due to a variety of factors including: rising energy costs, increased joblessness, lax conventional underwriting standards, falling home prices, and resetting interest rates for adjustable rate subprime mortgages.

The collapse of the subprime market and interest rate resets have brought a large volume of FHA refinanced mortgages. FHA began advocating for reform in 2006. Noting that the mortgage market had drifted away from FHA insured loans and the mandatory underwriting standards that accompany them, in February of 2006, as part of the President's FY 2007 budget submission, FHA submitted a modernization proposal to provide greater flexibility for FHA-funded mortgages. The request sought legislative reform to increase FHA loan limits, create a risk-based premium structure, enhance flexibility for downpayment requirements, simplify requirements for condominium loans, expand the use of reverse mortgages, and increase access to pre- and post-purchase counseling for low- and moderate-income homeowners. Most of these modifications were included in the **Housing and Economic Recovery Act of 2008** that was signed into law on July 30, 2008, which is discussed later in this section.

In FY 2007, FHA announced the ***FHASecure*** Program as a temporary measure to provide refinancing opportunities to homeowners with various types of Adjustable Rate Mortgages (ARMs). *FHASecure* gives qualified homeowners with non-FHA ARMs (whether current or delinquent and regardless of reset status) the ability to refinance into a FHA-insured mortgage. Homeowners who can no longer afford their mortgages and missed up to three monthly mortgage payments over the past 12 months are eligible for *FHASecure*. As a result, as of September 30, 2008, more than 368,000 homeowners refinanced through *FHASecure* since the program began.

Housing and Economic Recovery Act of 2008

On July 30, 2008, the President signed the **Housing and Economic Recovery Act of 2008** (**HERA**). This wide sweeping legislation implements many of the reforms recommended in the FHA Modernization package that was included in the President's FY 2007 budget. It also makes broad changes which lawmakers deemed necessary for correcting problems in the mortgage market, as evidenced by the increasing number of foreclosures and the consequent deterioration of the credit market.

In addition to provisions mandating FHA's involvement in helping homeowners to retain their homes despite recent mortgage payment defaults, HERA established provisions for the prosecution of mortgage fraud, and provided tax credits for certain mortgagors of both single family and multifamily homes. HERA also greatly increased FHA's limits on size of loans, aggregate amount of loans, and numbers of loans they could insure.

One provision of HERA is the creation of the *HOPE for Homeowners (**H4H**) Program*, which allows FHA to insure up to $300 billion in mortgages to assist homeowners to refinance with FHA to avoid foreclosure. H4H was implemented through a major program effort by FHA management, with support from the Department of the Treasury, the Federal Reserve Board, the Federal Depositors Insurance Corporation, and the Office of Management and Budget. The H4H program is operational, available to all FHA-approved mortgage lenders, and should serve the borrowers most in need of the refinancing option it provides. The program has features useful for those with no other choice than foreclosure. Currently, FHA management is engaging in industry outreach to mortgage lenders and servicers to explain underwriting and servicing policies of this program and will be training lenders on the new H4H.

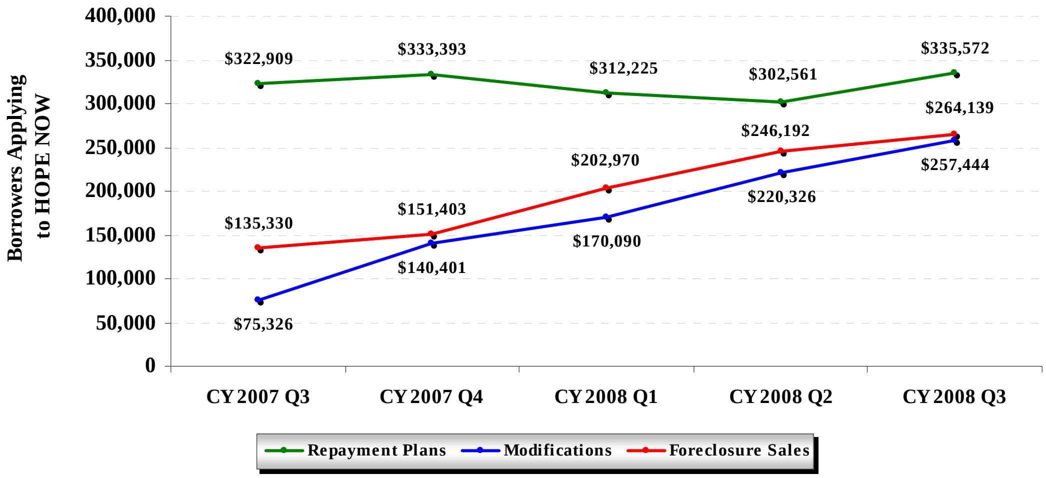
Finally, HERA established the Federal Housing Finance Agency (FHFA) which consolidates the oversight of the Government Sponsored Enterprises (GSE) Fannie Mae and Freddie Mac (formerly provided by the Office of Federal Housing Enterprise Oversight (OFHEO) within HUD), as well as the Federal Home Loan Banks. The GSE oversight goals, as well as the staff, office equipment, and supplies of OFHEO, were transferred to FHFA. In addition to providing for improved supervision, HERA requires the Federal Housing Finance Agency to take prompt corrective action when needed and to enforce regulations governing GSE activities.

More information on the Office of Housing is available at http://www.hud.gov/offices/hsg.

HOPE NOW

In October 2007, HUD joined with the Department of the Treasury and mortgage and banking officials to help form **HOPE NOW**, a private, independent coalition for counseling troubled homeowners regarding refinancing or restructuring their loans to avoid foreclosure. This expanded HUD's Housing Counseling outreach activities significantly as the coalition began to assist affected homeowners. In the chart below, based on national data from HOPE NOW, the Repayment Plans and the Modifications together represent homeowners who have avoided foreclosure through workout plans made with HOPE NOW assistance. In FY 2008 over 2,000,000 homeowners (about 70 percent of those who have sought counseling) avoided foreclosure through HOPE NOW.

Borrower Loan Workout Plans and Foreclosures
(Calendar Quarterly Data)



Many foreclosures are being prevented without a major restructuring of debt, and many lenders are willing to take actions to keep homeowners solvent. HOPE NOW counselors are all HUD intermediaries and are approved by HUD to provide Housing Counseling.

GINNIE MAE

Primary Focus: Increase Homeownership Opportunities

Major Programs: Mortgage-Backed Securities Guarantees

FY 2008 Budget Authority
Gross Budget Authority: $8.25 Million for Salaries and Expenses
Commitment Authority: $258.3 Billion
Mortgage-Backed Securities Income and Interest Income: $1.0 Billion
Ginnie Mae Securities Outstanding: $576.8 Billion
Authorized Staffing: 69 Full Time Equivalent

Performance Indicators
Number of Measures: 4 Number Met: 3 Number Missed: 1

Program Web Address: http://www.ginniemae.gov

Under the umbrella of HUD's efforts to promote affordable homeownership, the Government National Mortgage Association, commonly known as Ginnie Mae, has been effectively working in the secondary housing market to channel funds to lenders, enhancing the availability of funds for new mortgages and reducing the mortgage interest rates consumers pay. In the current uncertain environment of the housing crisis and financial crisis due to mortgage foreclosures, Ginnie Mae is strong and stable.

History of Ginnie Mae

In 1968, Congress established Ginnie Mae as a government corporation within the Department of Housing and Urban Development. Ginnie Mae revolutionized the American housing industry in 1970 by pioneering the issuance of Mortgage Backed Securities (MBS). By pooling packages of qualifying FHA, VA (Veterans Affairs), U.S. Department of Agriculture (USDA) Rural Development Housing and Community Facilities programs, or PIH (Public and Indian Housing - HUD) mortgages and converting them into securities, Ginnie Mae guarantees investors the timely payment of principal and interest on these securities.

Since its inception, Ginnie Mae has guaranteed approximately $2.9 trillion in MBS, providing homeownership for millions of households by securitizing government-insured loans.

Until the recent government takeover of Fannie Mae and Freddie Mac under a conservatorship arrangement, Ginnie Mae securities were the only MBS that offered the full faith and credit guaranty of the United States government.

Ginnie Mae and the Housing Crisis

The subprime collapse did not damage Ginnie Mae in the way that it did Fannie Mae and Freddie Mac. There are several reasons why.

1. Ginnie Mae securitizes loans that are insured by FHA, VA, USDA, and PIH (HUD). Thus it is able to offer investors a MBS that is backed by the full faith and credit of the United States government. Not only are the underwriting standards for these loans very high, but the backing gives Ginnie Mae an edge in times of market insecurity.
2. Ginnie Mae has high standards for the lenders they service.
3. Ginnie Mae has always taken a very conservative approach to investment and risk.

For these reasons, Ginnie Mae experienced a rise in the level of MBS issuance from $85.0 billion in FY 2007 to $220.6 billion in FY 2008, increasing its market share from 4 percent to 19 percent.

As the credit crisis began to swell, and FHA began to develop programs to bolster homeowners with delinquent loans, Ginnie Mae responded by creating new MBS pools to accommodate *FHASecure* delinquent loans and FHA higher balance loans, thus enabling even more borrowers to qualify for safe, affordable loans. With FHA's new programs and increasing market share, and with the increasing prominence of Ginnie Mae in the secondary market due to problems affecting the mortgage markets, Ginnie Mae has also taken specific actions to establish stability and assure confidence in Ginnie Mae's products.

Ginnie Mae has created a position of Chief Risk Officer responsible for establishing an overall risk governance structure and providing an independent evaluation of all risk management activities. The Chief Risk Officer evaluates lender eligibility requirements such as net worth and fidelity bonding, oversees standards for commitment authority, and monitors matching policy.

An Issuer Review Board (IRB) was also created to evaluate and approve decisions for risks that exceed the established standards or guidelines. The IRB reviews applications for new issuers (with authority to recommend by program area if overall standards are not met), reviews mergers and acquisitions, and reviews transfers of issuer responsibility.

A Risk Committee was created, composed of senior management, to address decisions regarding corporate risk issues affecting business functions, back office operations, financial statements, compliance risks, internal controls of policies and procedures that ensure strategy and management directives are carried out at all levels, monitoring controls, and independent reviews.

Ginnie Mae's recent volume increases will set the tone for the future of the secondary market and the strategies that will be needed to maintain high liquidity and stability for the sake of America's homebuyers. With the security of guaranteed, fixed, and timely interest and principal payments – regardless of declines in the housing market, increases in unemployment or difficulties at issuing financial firms – investments in Ginnie Mae securities are among the safest on the market.

PUBLIC AND INDIAN HOUSING

Primary Focus: Promote Decent Affordable Rental Housing

Major Programs: Section 8 Tenant-Based Rental Assistance, Public Housing Operating and Capital Funds, and Indian and Native Hawaiian Housing Block Grants and Loan Guarantee Funds

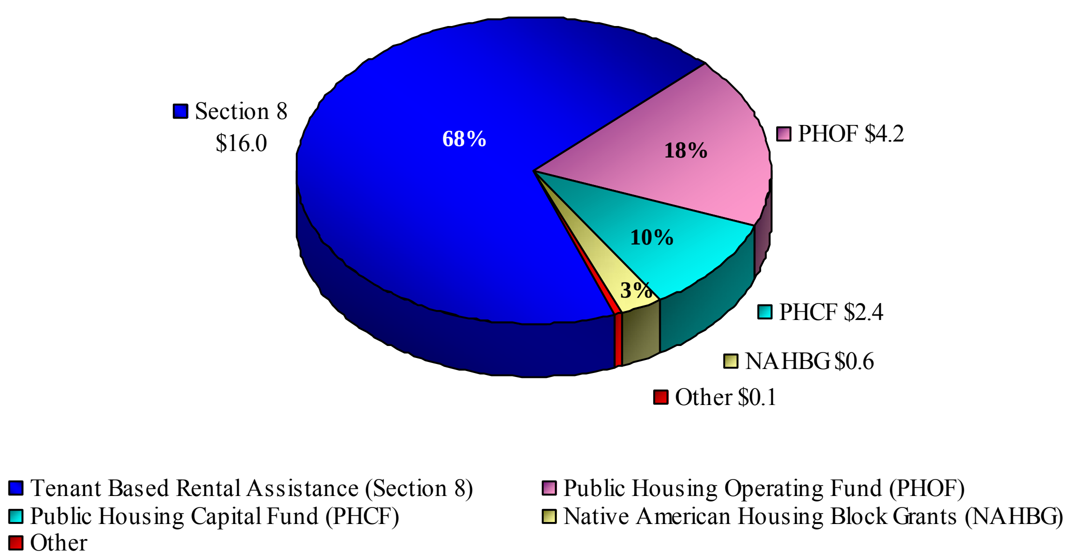
FY 2008 Budget Authority
Gross Budget Authority: $23.3 Billion
Authorized Staffing: 1,513 Full Time Equivalent

Performance
Number of Measures: 11 Number Met: 11 Number Missed: 0

Program Web Address
http://www.hud.gov/offices/pih/index.cfm

PIH's mission is to ensure safe, decent, and affordable housing for low-income households. PIH's success is measured by the number of American households that receive housing assistance in safe and secure units, and ensuring the financial stability of PHAs. During FY 2008, approximately 3.2 million households were assisted through PIH's programs.

PUBLIC AND INDIAN HOUSING
Gross Budget Authority FY 2008 ($23.3 billion)
Dollars In Billions



Additionally, PIH contributes to the strategic goal of Promoting Homeownership through the homeownership option of the Housing Choice Voucher/Housing Certificate Fund, the Indian and Native Hawaiian Block Grants, and through its Section 184 and 184A mortgage guarantee programs.

PIH administers $23.3 billion (43 percent) of HUD's annual discretionary budget authority for the benefit of low-income households. One of the Department's larger programs, Section 8 Housing Choice Vouchers, has been recognized as a cost-effective means for delivering decent, safe, and affordable housing to low-income families, serving approximately 2.1 million households through vouchers administered by more than 2,400 PHAs. These vouchers assist eligible families to obtain housing in the private market, and in a neighborhood of their choosing. This program appropriates funds for PHAs on a budget-based system, thereby making the PHAs more accountable in managing their budgets. HUD is in the process of streamlining the Section 8 program to make it more results-oriented. The initial analysis of the needed changes has been conducted and the proposed rule was developed and is in review.

One of HUD's priorities is to increase the PHAs utilization of voucher funds provided by the Department. HUD has noted an increase in the utilization rate from 90.0 percent in FY 2006, to 91.7 percent in FY 2007, and to 93.3 percent in FY 2008. (For more detailed information, see Indicator B.16.) Although this is an improvement, HUD still expects much greater utilization of these funds. To achieve improved utilization in the future, HUD plans to continue outreach to PHAs and to link future administrative fee payments to PHA leasing levels.

A continuing challenge related to all of HUD's rental housing assistance programs – including the Housing Choice Voucher and Public Housing Programs – is the issue of improper payments. HUD has been a government leader in addressing this issue, reducing its improper payment rate from an estimated 17.1 percent in 2000 to 3.5 percent today, and was the first Department to receive a Status Score of Green for this President's Management Agenda Initiative from OMB. Further details, including specific changes to address this issue within the PIH programs, can be found in Section 4 under Improper Payment Information Act Reporting and in Section 2, Indicator E.3.

PIH also distributes part of its annual budget authority to PHAs through Public Housing Operating Funds and Public Housing Capital Funds. These programs serve almost 1.1 million households. Given the significance of the resources and responsibilities entrusted to the PHAs, HUD has established comprehensive remote monitoring systems to assess performance and the need to target on-site monitoring, technical assistance, or other intervention actions to improve performance. Additionally, HUD provides funding for Native American families through block grant and loan guarantee programs.

River Garden Community new homeowners Lillie Daniels and her husband Ronald Craig welcome Secretary Steve Preston to their home in New Orleans. Daniels and Craig moved into their new home on May 1 after living in Memphis, Tenn. following Hurricane Katrina.

Operating Funds are provided to over 3,100 PHAs to assist them in meeting public housing project and management expenses such as administration, routine maintenance, anti-crime and anti-drug activities, resident participation in management, insurance costs, energy costs, and other costs, as appropriate, related principally to the operation of management of mixed finance projects. In FY 2008, the Public Housing Operating Fund was appropriated $4.2 billion to carry out its mission.

One of the largest expenses incurred by a PHA is its energy costs. During FY 2008, energy costs continued to escalate. To address the rising energy costs, HUD is:

- promoting energy efficiency nationwide;
- building HOPE VI developments to a high level of efficiency;
- improving tracking and monitoring of energy efficiency in public housing; and
- stream-lining energy performance contracting in public housing.

Since 2002, PIH's aggressive outreach program to promote energy performance contracts, for which PIH received a 2008 Presidential Leadership Award for Energy Management, has resulted in projected annual savings of $103 million. An example of an aggregate project is the Danbury Housing Authority, CT where projected annual savings of $65,000 for 12 years are expected from a $314,500 contract.

The "Public Housing Cost Study" recommended a transition to asset management to increase the focus and accountability of PHAs for each of their individual public housing properties as a valuable low-rent real estate asset. FY 2008 was the second year of the new Operating Fund formula, which requires conversion to asset management. Asset management includes adoption of project-based budgeting, accounting, and asset management to align PHA accounting and management practices to those used by private industry for PHAs with 400 or more units. Concurrent with the start of their fiscal year cycle, certain PHAs began implementation of project based accounting in FY 2007. In FY 2008, PHAs were funded via individual asset management projects for the first time instead of being funded at a PHA-wide level, and are required to fully implement asset management by FY 2011. As of the end of FY 2008, 99 percent had implemented asset-based accounting (For more detailed information, see Indicator B.25) and 258 PHAs (eight percent) had completed the conversion to asset management, exceeding the goal by 60 percent. (For more detailed information, see Indicator B.26.)

Recognizing that the implementation of asset management by PHAs is a complex process, HUD has provided guidance and assistance to PHAs through issuance of a number of timely notices, both informational and program-specific, development of a comprehensive training program, and web-site access to these and other tools to assist during the transition phase. These notices provided detailed information to the PHAs regarding the steps needed to complete the transition to asset management.

Additionally, through the Department's physical housing assessment process, PHAs are provided information on the physical condition of every property in their inventory. PHAs are also provided with an analysis of the most common deficiencies identified with a comparison to the prior inspection so that PHAs can monitor their progress in correcting identified deficiencies. HUD's field office staff used the information obtained from the physical assessment process in their risk management activities and to prioritize their monitoring and technical assistance to those PHAs that present the greatest risk to the program. As of September 30, 2008, the percentage of public housing units meeting HUD's physical condition standards was 84.5 percent, substantially meeting the goal of 85.0 percent. (For more detailed information, see Indicator B.17.) Once the Department has completed the transition to asset management, the physical condition goal will be tracked on a property level basis.

In addition to the physical condition of PHA properties, the Department also evaluates the performance of the PHA on management operations, financial condition, and resident satisfaction using its Public Housing Assessment System. The composite score of these four factors, if below 60 percent, or a single factor below 18 percent, results in the PHA being classified as "troubled." The number of PHAs in this category dropped from 161 as of October 1, 2007 to 95 at the end of the fiscal year, a reduction of 77.4 percent. (For more detailed information, see Indicator B.19.)

Public Housing Capital Funds were provided to over 3,100 PHAs with the average grant amounting to $750,000 during FY 2008 to finance capital improvements including the development, financing, and modernization of public housing developments and for management improvements. The Public Housing Capital Fund account protects and enhances the value of this important affordable housing resource. Without this inventory, more families would be at risk of facing possible worst case housing needs (Worst-case housing needs are unassisted families and individuals with "very low-incomes" (i.e., less than 50 percent of area median income)) and would be further at risk of homelessness.

Under the Capital Fund Financing Program, a PHA may borrow funds from the private markets, pledge a portion of its future year annual capital funds, subject to the availability of appropriations, and then repay the financing as they receive their capital funds. This allows PHAs to leverage resources to meet pressing capital needs. During FY 2008, the Office of Capital Improvements approved approximately $504 million of leveraged funds through the Capital Fund Financing Program. This approval provided 15 PHAs with funding to modernize and develop public housing, thus protecting and enhancing the affordable housing stock.

Promoting Homeownership

HOPE VI, Section 184 Loan Guarantee program, the Section 184A Loan Guarantee program for Native Hawaiians, and the homeownership option under the Housing Choice Voucher, Family Self-Sufficiency, and Moving to Work programs are each focused on a particular housing program delivery constituency. In total, they helped 9,314 households become homeowners in FY 2008, exceeding the goal of 8,000 for the year. The results for each program can be found in Section 2 under Indicator A.1.

Disaster Assistance

In August and September, 2008, Hurricanes Ike and Gustav struck the United States, causing catastrophic damage to property, loss of life, and the displacement of tens of thousands of individuals from their homes and communities. On September 23, 2008, HUD and Federal Emergency Management Agency executed an Interagency Agreement under which HUD shall act as the servicing agency of Disaster Housing Assistance Program - Ike, and will begin administration of the program effective November 1, 2008. HUD will once again utilize its existing network of local PHAs to administer tenant-based rental assistance and provide case management services, and security deposit and utility deposit assistance to impacted families under Disaster Housing Assistance Program - Ike. PHAs administer the Housing Choice Voucher Program and, as a result, have the necessary local market knowledge and expertise in assisting families through a tenant-based subsidy program. In addition, through their prior administration of the Disaster Housing Assistance Program, the Disaster Voucher Program and the Katrina Disaster Housing Assistance Program, PHAs are experienced in working with significant numbers of families that have been displaced by disasters. Pursuant to the Federal Emergency Management Agency's grant authority, grants will be provided to local PHAs to administer Disaster Housing Assistance Program - Ike on behalf of Federal Emergency Management Agency. PHAs will make rental assistance payments on behalf of eligible families to participating landlords for a period not to exceed 17 months, commencing November 1, 2008 and ending no later than March 2010.

Floods in Wisconsin, Spring 2008

The Office of Public and Indian Housing was also recognized for its disaster relief efforts. Its **National Housing Locator (https://hudapps.hud.gov/nhls/)** was the nation's first National Housing Locator system for rental housing assistance in disaster areas. This intergovernmental web site was launched in January 2007 as a direct response to lessons learned from Hurricane Katrina, most notably the lack of a nationwide, single point of entry, easily searchable system identifying available rental housing in times of disaster such as was experienced in this year's floods in the Midwest, and by Hurricanes Gustav and Ike in the South.

COMMUNITY PLANNING AND DEVELOPMENT

Primary Focus: Strengthen communities and expand economic and community development opportunities for low- and moderate-income households

Major Programs: Community Development Block Grants, Affordable Housing, and Special Needs Assistance

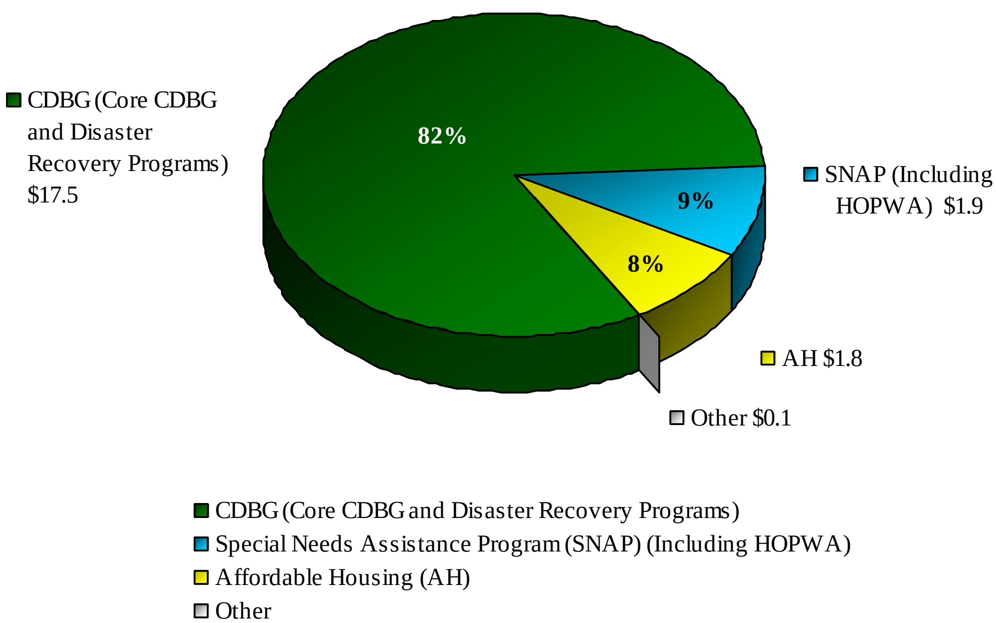
FY 2008 Budget Authority:
Gross Budget Authority: $21.3 Billion
CPD Core Programs: $7.6 Billion
CPD Disaster Relief: $13.7 Billion
Authorized Staffing: 777 Full Time Equivalent

Performance Indicators:
Number of Measures: 19 Number Met: 15 Number Missed: 4

Program Web Address: http://www.hud.gov/offices/cpd/about/cpd_programs

The Office of Community Planning and Development (CPD) seeks to develop viable communities by promoting integrated approaches that expand economic opportunities for low- and moderate-income persons, and provide decent housing with a suitable living environment. The primary means towards this end is the development of partnerships among all levels of government and the private sector, including for-profit and non-profit organizations.

COMMUNITY PLANNING AND DEVELOPMENT
Gross Budget Authoriy FY 2008 ($21.3 billion)
Dollars In Billions



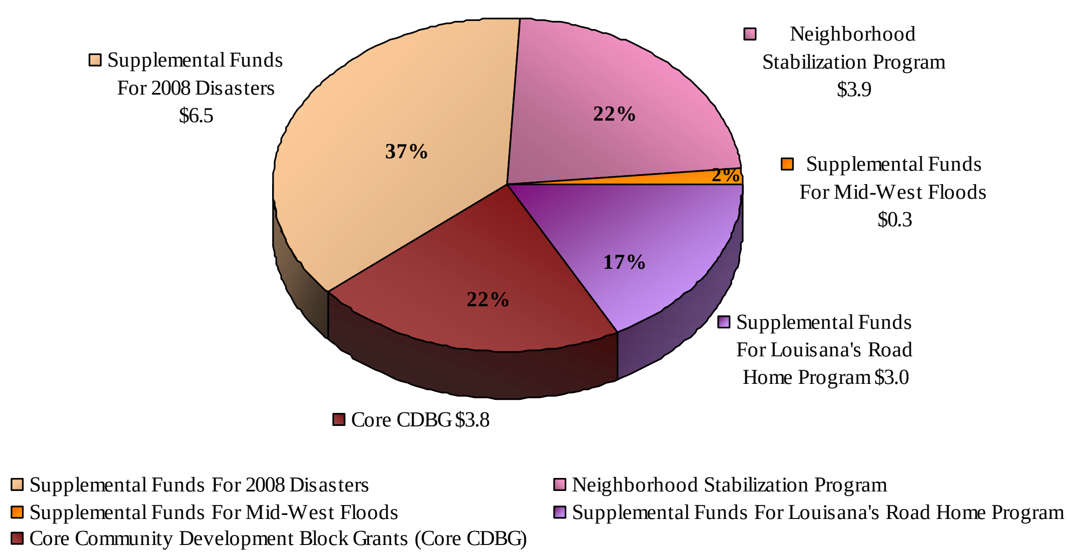
CPD seeks to encourage empowerment of local residents by helping to give them a voice in the future of their neighborhoods; stimulate the creation of community based organizations; and enhance the management skills of existing organizations so they can achieve greater production capacity. Housing and community development are not viewed as separate programs, but rather as among the myriad of elements that make up a comprehensive vision of community development. These groups are at the heart of a bottom-up housing and community development strategy.

While CPD does offer flexibility in its programs, it continuously monitors (remote and on-site) to ensure compliance with applicable Federal and HUD regulations and requirements and to ensure performance standards are met. In FY 2008, the CPD field office staff monitored 1,076 grantees, or 22 percent of 4,789 active competitive and formula grantees, thereby exceeding the goal of 20 percent. (For more detailed information, see Indicator E.5.) Monitoring measures the effectiveness of grantees' financial management controls and ensures program compliance with applicable Federal and HUD rules and regulations, and serves to deter and prevent fraud, waste, abuse and mismanagement of funds. It also identifies whether HUD resources are targeted to improve underserved communities.

The primary CPD programs consist of Community Development Block Grants, Affordable Housing program, and Special Needs Assistance. A description of these programs and their major accomplishments and challenges follows.

Community Development Block Grants (CDBG)

Core CDBG And Disaster Recovery Programs ($17.5 billion)
Dollars In Billions



While the CDBG program has generated notable results throughout its history, HUD is pursuing changes to the program to further improve HUD's assistance to state and local governments.

The CDBG program has remained essentially unchanged since its inception in 1974. HUD submitted a proposal to the Congress to reform the program. The implementation of this reform legislation is one of HUD's goals, but is dependant upon Congressional action. (For more detailed information, see Indicator C.7.) The proposed legislation includes:

- CDBG formula reform intended to target funding to the nation's neediest communities;
- A provision for challenge grant funds that will be awarded to communities that show the greatest improvements in measures of community livability and investment; and
- Performance measurement provisions to hold grantees more accountable for meeting their own goals.

The CDBG program operates to ensure suitable affordable housing, to administer grants to the most vulnerable communities and create jobs through the expansion and retention of businesses. CDBG is a significant mechanism that assists local governments to address exigent problems endured by their communities. Since its inception in 1974, the CDBG program has paid approximately $141 billion to state and local governments, to help strengthen communities across the nation.

In FY 2008, CDBG's total budget was approximately $17.5 billion. This represents an increase of 373 percent from FY 2007, primarily due to a $13.7 billion budget addition, comprised of disaster supplemental emergency funds for Louisiana ($3.0 billion), Mid-west floods ($300 million), Neighborhood Stabilization Program for foreclosed homes ($3.9 billion), and supplemental funds for 2008 disasters ($6.5 billion as enacted). Furthermore, HUD received FEMA mission assignments to staff their respective joint field offices and the disaster recovery centers to provide housing-related expertise and housing opportunities using the HUD National Housing Locator system.

The CDBG program can be classified into two parts, core CDBG and disaster recovery assistance. The ensuing discussion details the results and overall benefit to the general public.

Core CDBG Programs

The core CDBG program is comprised of three major programs: 1) Entitlement Communities, 2) State Programs, and 3) Section 108 Loan Guarantees.

The Entitlement Communities and State Programs provide grants to units of general and local government and states for the funding of local community development programs. Annual grant funds are awarded to entitlement communities containing metropolitan cities with populations of 50,000 and qualified urban counties with populations of at least 200,000. State programs are cities with populations of less than 50,000, except cities that are designated principal cities of Metropolitan Statistical Areas and counties with populations of less than 200,000. The program's primary objective is to develop viable urban communities by providing affordable and decent housing and a suitable living environment, as well as expanding economic opportunities to individuals of low- and moderate-incomes. One of the goals is to expend at least 90 percent of state and entitlement CDBG funds on activities that benefit low- and moderate-income persons. (For more detailed information, see Indicator C.6.) In FY 2008, the results were exceptional, with 95.6 percent benefiting those groups. Another goal is to eliminate 5,000 vacant, boarded up, or abandoned properties by the end of FY 2008. The elimination of these structures helps improve the quality of life of residents as the existence of these properties indicates a neighborhood in decline. CPD was very successful in regard to this goal, as 9,180 properties were demolished. (For more detailed information, see Indicator C.9.)

The Community Development Loan Guarantee (Section 108) is the loan guarantee provision of the CDBG program, which provides communities with a source of financing for economic development, housing rehabilitation, public facilities, and large-scale physical development projects. Section 108 allows local governments to leverage their CDBG funds into federally guaranteed loans large enough to pursue physical and economic revitalization projects that can renew entire neighborhoods. Projects funded with Section 108 commitments approved in FY 2008 will result in 6,491 jobs being created because of Section 108 loan guarantee assistance. In FY 2008, Section 108's authority level was $205 million, representing a 52 percent increase over the $135 million provided in FY 2007, which is below the historic rate of $2 billion dollars. (For more detailed information, see Indicator C.4.)

In FY 2008, CDBG grantees expended approximately $4.3 billion in grant funds and program income for programs and activities such as housing ($1.1 billion), economic development ($343 million), public improvements ($1.4 billion), public services ($466 million), and others ($1 billion).

In addition to HUD's core Community Development programs, Congress provided supplemental funding to HUD to provide support and relief to citizens and communities devastated by various disasters. This funding was provided to address the recovery efforts for hurricanes that occurred in 2005 (Katrina, Rita, and Wilma) and for the 2008 hurricanes and mid-west floods. A summary of these disaster recovery assistance programs follows.

Disaster Recovery Assistance (Gulf Coast States)

The Gulf Coast States are still recovering from the devastating hurricanes of 2005. Congress appropriated Disaster Recovery Assistance funds to HUD in 2005 and 2006 in the amount of $11.5 billion and $5.2 billion respectively, for the states of Alabama, Florida, Louisiana, Mississippi, and Texas to address the devastations of hurricanes Katrina, Rita and Wilma. In FY 2008, Congress appropriated an additional $3.0 billion for the State of Louisiana solely for the purpose of covering costs associated with otherwise uncompensated but eligible claims that were filed on or before July 31, 2007, under the *Road Home* program administered by the state in accordance with plans accepted by HUD's Secretary. The *Road Home* program is designed to provide compensation to its citizen homeowners affected by Hurricanes Katrina or Rita for the damages of their homes and is administered by the State of Louisiana.

All five Gulf Coast disaster grantees (states) have HUD approved action plans for their respective self-designed programs, to address a number of immediate and long-term needs including homeowner compensation programs, housing for renters, state and local infrastructure reconstruction, economic development, public services, rent support, and restoration of homeless services. Two years after the disasters, all five states have sustained progress towards assisting its citizens in recovering from the hurricane damages, and have helped low- to moderate-income individuals and communities affected by the disasters.

Ninety-six percent of the appropriated funds have been allocated to the states of Louisiana and Mississippi, with Louisiana receiving $13.4 billion and Mississippi $5.5 billion. Of the total $13.4 billion awarded to Louisiana, 75 percent of the monies are for the *Road Home* program. This program offers several options based on eligibility criteria and is targeted to assist homeowners, small-scale rental property owners, and building professionals. Fifty percent of the $5.5 billion awarded to Mississippi is for the *Homeowner Program*, which is designed to provide financial assistance to homeowners that were outside the flood plains. In FY 2008, Louisiana provided $7.1 billion to 118,335 *Road Home* applicants while Mississippi provided $1.7 billion to 23,651 *Homeowner Program* applicants.

The remaining CDBG funds for Louisiana and Mississippi are allocated for state and local infrastructure activities, restoration of homeless support and housing activities, public services, economic development, as well as other activities.

The aftermath of hurricane Katrina caused the Martin Luther King, Jr. Elementary School to be flooded in excess of 10 feet.

The CDBG disaster funds helped to renovate and rebuild the Martin Luther King, Jr. elementary school, which later re-opened in June 2007, making it the first school to re-open in the Lower Ninth Ward.

In support of affordable rental housing, the State of Louisiana has allocated $1.52 billion for the development of small rental housing and multifamily rental housing, representing over 18,000 affordable housing units. The State of Mississippi awarded $105 million to rehabilitate, reconstruct, or replace 2,965 public housing units, and allocated $262 million to the small rental assistance program for the development of over 3,400 housing units.

The hurricanes of 2005 severely affected Louisiana's and Mississippi's economic infrastructure. For example, Louisiana's fisheries industry suffered vast infrastructure damage, which precipitated a sharp decline in consumer consumption of fish, both in the commercial and retail industries. Studies initiated by the National Oceanic and Atmospheric Administration estimate that Hurricane Katrina alone generated more than $1.3 billion of economic loss to Louisiana's fishing industry. To assist this ailing industry, Louisiana has proposed funding approximately $9.75 million from the first supplemental appropriation to improve and expand infrastructure critical to the recreational and commercial fisheries industries, including, docks, icehouses, boat launches, processing and shipping facilities, boats and other necessary infrastructure.

The State of Louisiana has allocated another $330 million for economic development, including loan and grant capital for small firms, technical assistance to help companies adjust to the new business environment, and funding for tourism marketing to attract visitors and conventions. The State of Mississippi has allocated $1.25 billion for economic development, including $542 million for the Port of Gulfport. The Port was the third busiest container port in the Gulf of Mexico and the 17th busiest in the United States. Prior to Hurricane Katrina, for the month of December 2004, the Port exported and imported a total of almost 228,000 tons of cargo. For the month of December 2005, four months after the storm, the Port was able to move only 98,000 tons of cargo. Under these economic development programs, the State of Mississippi expects to create 8,898 jobs, including 5,400 for the Port of Gulfport.

The States of Alabama, Florida, and Texas comprise the remaining 4 percent of the total Gulf Coast appropriated funds, with $781 million in funding for these states. In all three states, funding is targeted primarily to housing, infrastructure, and public facilities.



After the hurricane storm damage: **(left)** east view and **(middle)** west view. New home from CDBG funds **(right)**.

The elderly husband and wife who own this single family home had lived at this address for seven years before the hurricane of 2005. After the hurricane's devastation, the husband lost his job as a local shipbuilder, and the family had no income. The family lived in a FEMA trailer for 2 years, after their house was deemed beyond repair and was condemned. They were later approved for a new home through the City of Bayou La Batre's HUD CDBG grant funds and stayed in a FEMA trailer on-site until construction of their home was complete.

2008 Hurricane Disasters

In addition to the Gulf Coast hurricane disasters of 2005, the effects of the strong spring storms in 2008 resulted in Congress appropriating $300 million in emergency disaster assistance for the Midwestern states which were affected by the floods in late spring. In addition, Congress appropriated $6.5 billion as enacted for disaster relief, long-term revitalization in federally declared disaster areas affected by hurricanes (including Ike and Gustav), floods and other natural disasters occurring during 2008.

Abandoned/Foreclosed Homes (*Neighborhood Stabilization Program*)

The **Housing and Economic Recovery Act of 2008** (The Act) provided $3.92 billion in emergency assistance to state and local governments to use for the redevelopment of abandoned and foreclosed homes and residential properties. The grant program is commonly referred to as the Neighborhood Stabilization Program (NSP). The NSP provides targeted emergency assistance to state and local governments to acquire and redevelop foreclosed properties that might otherwise become sources of abandonment and blight within their communities. State and local governments can use their neighborhood stabilization grants to purchase and rehabilitate homes and residential properties that have been abandoned or foreclosed upon in order to sell, rent or redevelop these properties, demolish blighted structures, redevelop demolished or vacant properties, and/or provide downpayment, closing costs or other assistance to help low-, moderate-, and middle-income households purchase these properties. In addition, grantees can create "land banks" to assemble, temporarily manage, and dispose of vacant land for the purpose of stabilizing neighborhoods and encouraging re-use or redevelopment of urban property.

The Act requires funds be allocated to states and units of general local government with the greatest need, as such need is determined in the discretion of the Secretary based on: 1) the number and percentage of home foreclosures in each state or unit of general local government; 2) the number and percentage of homes financed by a subprime mortgage related loan in each state or unit of general local government; and, 3) the number and percentage of homes in default or delinquency in each state or unit of general local government.

The NSP allocations were announced on September 26, 2008, and appear on HUD's website at **http://www.hud.gov/nsp**. In addition, HUD published a Notice in the *Federal Register* on October 6, 2008, that provides the details about the funding formula, grantee application procedures, and other rules and requirements specific to the administration of NSP funds. The Notice is also available on HUD's website.

AFFORDABLE HOUSING

The Office of Affordable Housing administers three separate programs designed to address the nationwide shortage of affordable housing. The HOME Investment Partnerships, Self-Help Homeownership Opportunity (SHOP), and Homeownership Zone programs provide federal resources directly to the state and local level for use in the development of affordable housing units, or to assist income-eligible households in purchasing, rehabilitating, or renting safe and decent housing.

HOME

The HOME program helps to expand the supply of decent, affordable housing for low- and very low-income families by providing grants to states and local governments called participating jurisdictions or "PJs". PJs use their HOME grants to fund housing programs that meet local needs and priorities. Forty percent of HOME funds are allocated to states and 60 percent are allocated to units of local government. PJs have a great deal of flexibility in designing their local HOME programs within the guidelines established by the HOME program statute and final rule. PJs may use their HOME funds to help renters, new homebuyers, or existing homeowners. Since its inception in 1990, the HOME program has acquired, constructed, or rehabilitated nearly 873,000 affordable housing units and nearly 198,000 tenants have received direct rental assistance.

In FY 2008, HOME's budget was $1.7 billion, which is expected to result in 85,350 units of affordable housing, through new construction, rehabilitation and acquisition, and which will assist 17,760 low-income households with tenant-based rental assistance. During FY 2008, 642 PJs used HOME funds to complete 30,999 new homebuyer units and/or directly assist homebuyer households. Additionally, 384 American Dream Down Payment Initiative (ADDI) recipients received ADDI funds to complete 4,209 new homebuyer units and/or directly assist first-time homebuyer households.

This 52-unit project, located in Cuyahoga County (Cleveland), was the first new Permanent Supportive Housing for the homeless. CPD HOME funding for this project included $500,000 from the Cuyahoga Housing Consortium and $1.25 million from the City of Cleveland.

The owner of this home is a single mother with 2 boys, and is a first time homebuyer. The home is an ENERGY STAR certified Heritage home designed to be sustainable and affordable for the future.

SPECIAL NEEDS ASSISTANCE

The Special Needs Assistance program's primary focus is to assist in the reduction of homelessness in the Nation, by funding programs to help persons who are homeless by offering permanent supportive housing. Special needs efforts also involve housing assistance for low-income persons living with HIV/AIDS.

Homeless Assistance Grants (HAG)

In FY 2008, the HAG program had a budget of approximately $1.6 billion, which represents approximately 8 percent of CPD's total budget. The goal of homeless assistance is to help homeless families and individuals achieve the outcome of staying in permanent housing and obtaining self-sufficiency, thereby reducing the number of homeless and chronically homeless persons in the Nation. To meet this goal, HUD funds a continuum of care—housing and services to meet all levels of need, from emergency shelter to transitional housing to permanent supportive housing. Congress requires that 30 percent of HUD's homeless assistance funding be allocated to permanent housing, and HUD's programs and policies support this requirement. For example, HUD strives to assist the homeless to remain in permanent housing for more than six months. Shelter Plus Care provides permanent housing assistance, while communities secure an equal level of funding for a variety of supportive services from other sources. This combination ensures that residents receive the housing and services they need to maintain stable permanent housing and to make progress towards self-sufficiency.

In FY 2008, HUD exceeded its targeted assistance goals to reduce the effects of chronic homelessness. The Department achieved 75.1 percent of formerly homeless persons remaining in permanent housing for at least six months. This achievement is 3.6 percentage points, or 5 percent above the target of 71.5 percent. Similar progress was evidenced in transitional housing, wherein 71.1 percent of homeless persons moved from transitional housing into permanent housing. This is an increase of 7.6 percentage points, or 12 percent increase above the 63.5 percent target for FY 2008. Employment of homeless persons exiting permanent housing also saw an increase of 2.9 percentage points, or 15 percent, from its targeted goal of 19 percent, thereby yielding 21.9 percent for FY 2008. Details for each of these areas can be found in Section 2 of this report.

Housing Opportunities For Persons With AIDS Program (HOPWA)

HOPWA assists persons with HIV/AIDS maintain stable housing as a base to access HIV treatment and other care. HOPWA is the only federal program dedicated to address the housing needs of persons living with HIV/AIDS and their families.

One of the primary purposes of HOPWA is to reduce the risk of homelessness for persons living with HIV/AIDS. HOPWA provides 1) support to develop and operate community residences and other housing facilities, 2) short-term rent, mortgage, and utility assistance, which is a limited housing payment provided to homeowners and renters to prevent homelessness, and 3) tenant-based rental assistance.

In FY 2008, HOPWA's budget was $300 million which allowed HUD to provide assistance to 127 jurisdictions nationwide. Initial data reports indicate that this assistance helped 92 percent of households receiving assistance attain housing stability. (For more detailed information, see Indicator C.13.) Approximately 21,405 households received support through HOPWA's permanent housing projects, another 40,805 received benefits to reduce risks of homelessness under the short-term and transitional housing projects and 35,253 eligible persons benefited under housing assistance leveraged from other state, local or private sources operating under the community's HIV housing efforts. (For more detailed information, see Indicator B.1.)

OTHER CPD PROGRAMS

HUD works with the public and private sectors, as well as not-for-profit organizations, to provide financial and technical assistance to local communities to develop and implement their own economic development and community revitalization strategies. In an effort to lend greater weight to local economic development priorities, the Department has adopted a streamlined process for the approval of requests for assistance, moving significant decision-making authority closer to communities in need, through our Community Planning and Development field offices. HUD's programs include (1) Empowerment Zone and Renewal Community, which encourage businesses to open and expand and to hire local residents, (2) Rural Housing and Economic Development, which was established to assist nonprofit organizations in rural communities across America, and (3) the Brownfield Economic Development Initiative, which assists in returning to productive use real property that is abandoned, idled or under-used and where expansion or redevelopment is complicated by the presence or potential presence of environmental contamination. The Empowerment Zone and Renewal Community employment credits offer financial incentives to employers to hire residents of Empowerment Zones and Renewal Communities. Employers who use these credits regularly save a great deal at tax time, which helps them to retain current employees and make additional hires. In FY 2008, sole proprietors claimed approximately $121 million in Empowerment Zone and Renewal Community employment credits, which is $46 million less than the FY 2008 goal of $167 million. The $121 million represents a 22 percent reduction from the actual total of approximately $155 million from the previous year. (For more detailed information, see Indicator C.8.) This reduction was surprising, since employment credit claims in the

Empowerment Zones and Renewal Communities had been steadily increasing for several years, sometimes by more than 20 percent annually.

FAIR HOUSING AND EQUAL OPPORTUNITY

Primary Focus: Create Equal Housing Opportunities

Major Programs: Fair Housing Assistance Program, Fair Housing Initiatives Program and Enforcement

FY 2008 Budget Authority:
Gross Budget Authority: $50 Million
Authorized Staffing: 583 Full Time Equivalent

Performance Indicators:
Number of Measures: 7 Number Met: 6 Number Missed: 1

Program Web Address: http://www.hud.gov/offices/fheo/index.cfm

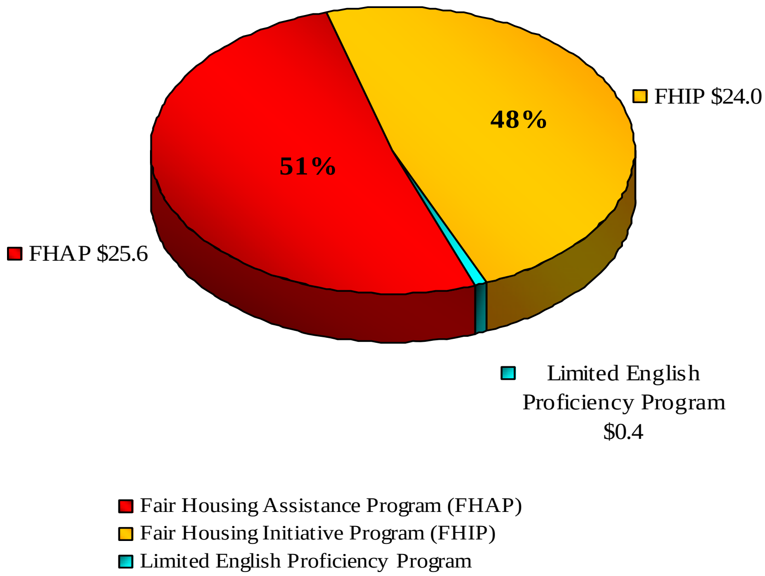
The Office of Fair Housing and Equal Opportunity (FHEO) strives to create equal housing opportunities by enforcing Federal laws that prohibit discrimination in housing on the basis of race, color, religion, sex, national origin, disability, familial status, and age.

Discrimination in mortgage lending is also prohibited by the federal **Fair Housing Act**, and FHEO actively enforces those provisions of the law. The Fair Housing Act makes it unlawful to engage in the following practices based on race, color, national origin, religion, sex, familial status, or handicap (disability):

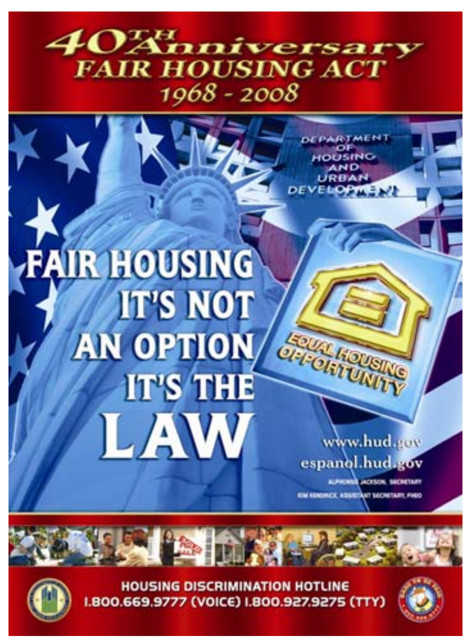
- Refuse to make a mortgage loan;
- Refuse to provide information regarding loans;
- Impose different terms or conditions on a loan, such as different interest rates, points, or fees;
- Discriminate in appraising property; and
- Refuse to purchase a loan or set different terms or conditions for purchasing a loan.

FHEO, with an FY 2008 appropriation of $50 million, administers two major funding programs to assist in reducing the incidence of housing discrimination: the Fair Housing Assistance Program and the Fair Housing Initiatives Program. In addition, through its Limited English Proficiency program, FHEO provides translation resources for its programs and activities to individuals with limited English communications skills.

FAIR HOUSING AND EQUAL OPPORTUNITY
Gross Budget Authority FY 2008 ($50 million)
Dollars In Millions



The first step towards reducing discrimination and unfair practices is to increase public awareness of fair housing laws, housing discrimination, lending discrimination and predatory lending, as well as educating the public about what they can do and where to go for assistance. HUD has continued to surpass its education and awareness goals, conducting 1,783 education and outreach events during FY 2008. These events reached nearly 300,000 people. (For more detailed information, see Indicator D.2.)



Enforcement of fair housing laws is crucial to enhancing housing opportunities for all people of the United States. The ability to provide a fair, effective, expeditious, and efficient fair housing complaint process is essential to maintain public confidence that victims of housing discrimination will receive relief from discriminatory housing practices and that violators will be disciplined. Victims of housing discrimination need to know that they will receive timely relief from discriminatory housing practices. Efficiency and timeliness of complaint processing is a major focus for the Department's FY 2008 goals. Several goals track both the progress in meeting a 100 day standard for completing cases and the progress in closing cases aged beyond 100 days. As a result, the Department established a goal to complete 55 percent of all discrimination cases within 100 days. In FY 2008, the Department completed 60 percent of new complaints filed within 100 days, exceeding its target by 5 percent. The Department also exceeded its goals related to “aged” cases during the year. (For more detailed information regarding both of these goals, see Indicator D.1.)

The Department did not achieve its goal related to Fair Housing Assistance Program agencies closing 53 percent of fair housing complaints referred by HUD within 100 days, closing only 50 percent. The principle reason that HUD fell short in meeting this goal is that some jurisdictions have overriding concerns that require them to focus on goals other than completing cases within 100 days. For example, the California Department of Fair Employment and Housing is required under California Fair Employment and Housing Act to complete its investigations within 365 days, or it loses jurisdiction over the case and can no longer investigate it. This statutory requirement forces California Department of Fair Employment and Housing to focus on completing all of its cases within 365 days, rather than most of its cases within 100 days. This has a significant impact on the overall performance of the program because the California Department of Fair Employment and Housing is the largest agency in the Fair Housing Assistance Program, responsible for processing approximately 15 percent of all Fair Housing Assistance Program cases in FY 2008. (For more detailed information, see Indicator D.1.)

HUD also met its goal to develop a database of accessible housing units to establish a framework for monitoring the efforts of Public Housing Authorities to increase the number of HUD-assisted units made accessible as a result of Voluntary Compliance Agreements. (For more detailed information, see Indicator D.3.)

HUD investigates complaints of housing discrimination, including discriminatory lending complaints, at no cost to individuals who believe they have experienced discrimination. Individuals should visit our housing discrimination complaint website (http://www.hud.gov/offices/fheo/complaint-process.cfm) to learn more about the complaint process.

OTHER ORGANIZATIONS IN HUD

Healthy Homes and Lead Hazard Control

(http://www.hud.gov/offices/lead/)

The elimination of lead poisoning in children as a major public health problem by 2010 is one of the President's and Secretary's priorities. This effort is the responsibility of the Office of Healthy Homes and Lead Hazard Control (OHHLHC). The OHHLHC, with an FY 2008 appropriation of $145 million, directs programs that address the health and safety needs of homes: the Lead Hazard Control Program, the Healthy Homes Initiative, and enforcing lead safety regulations. The Office provides funds to state and local governments, and to the private sector, to develop and implement cost-effective ways to reduce lead-based paint and other residential safety and health hazards. The Office enforces the Lead Disclosure Rule and supports enforcement by Program Offices of the Lead Safe Housing Rule.

HUD's Lead Hazard Control Program is the central element of the President's program to eradicate childhood lead-based paint poisoning. In the 1990 to 1994 time period, the number of children with elevated blood lead levels was 890,000. As of the end of FY 2008, that number was 215,000. HUD provides grant funds targeted to help low-income, privately owned homes that are most likely to expose children to lead-based paint hazards. HUD awards grants in several categories, including: grants to state and local jurisdictions under the Office's largest Lead Hazard Control grant programs (for Lead-Based Paint Hazard Control grants and Lead Hazard Reduction Demonstration grants, the latter going to areas with the highest need); Operation Lead Elimination Action Program (LEAP) grants to the private sector to leverage funds for making homes lead-safe; Lead Outreach grants to promote public education and awareness of lead hazards; and Lead Technical Studies grants to support research on evaluating and controlling lead hazards more efficiently. The goal to reduce the number to less than 220,000 children that had elevated blood lead levels was met. HUD also exceeded its goal of making 11,500 housing units lead-safe by 1,069 units as a result of its grant awards program. (For more detailed information on these goals, see Indicators C.20 and C.21.)

The pavilion is a transportable model home that is utilized to educate the public about how to keep a safe and healthy home.

HUD's Healthy Homes Initiative responds to the environmental hazards in the home that harm millions of children each year. The Initiative takes a comprehensive approach by implementing grants and contracts that address housing-related hazards in a coordinated fashion, rather than addressing a single hazard at a time. One of many ways of making homes healthy is reducing the level of allergy-inducing substances (allergens) in house dust; these are associated with debris from pets, dust mites, cockroaches, and rodents.

A **"Healthy Homes for Healthy Kids"** campaign was initiated by HUD in April of 2006. This three-year, 30-city outreach effort will inform parents about health and safety hazards in the home. This outreach effort includes providing information on lead paint, mold, moisture, and pests like mice and cockroaches.

Enforcement of lead-based paint regulations in pre-1978 housing being rented, or sold, or being assisted by HUD is carried out by this Office. The Office also provides public outreach and technical assistance, and conducts technical studies to help protect children and their families from health and safety hazards in the home.

Lead poisoning is the number one environmental disease affecting children. These children, especially those less than three years old, are vulnerable to permanent developmental problems due to the effect of lead on the nervous system. Addressing this problem responds to the President's and Secretary's priority effort to eliminate lead poisoning in children. These results are directly aligned to the accomplishments of HUD grantees under its lead grant programs and of HUD's regulatory enforcement program.

Faith Based and Community Initiatives

http://www.hud.gov/offices/fbci/

The Center for Faith-Based and Community Initiatives is one of 10 such centers established by the President in Cabinet level agencies. The Center's goal is to implement the President's vision of a compassionate community, where faith-based and community organizations work with government to help the needy in a more effective manner. One of the key principles in this Presidential initiative is that all groups, whether religious or secular, should compete on a level playing field when applying for federal funds. As a result, an important part of the Center's work is empowering faith-based and community organizations to apply for HUD grants. The Center does not make decisions on awarding grants, nor is there any preference for faith-based organizations. Instead, the Center works to remove unnecessary barriers in order to fully engage these organizations as partners in fulfilling HUD's mission. One of the Center's activities to assist organizations to obtain federal grants is through grant writing training sessions. In FY 2008, 68 training sessions were held, 38 more than the goal. (For more detailed information, see Indicator F2.1.) The Center also works to bring together state, local and federal community partners within the participating area to build bridges and form partnerships with faith-base and community organizations through its Unlocking Doors Initiative. (For more detailed information, see Indicator F.3.) In collaboration with the Office of PIH, the HOPE VI Mentoring pilot project aims to encourage Public Housing Authorities to enlist area faith-based and community organizations to supply mentors for public housing residents in order to increase the residents' Fair Isaac Corporation (FICO) credit scores, attain General Education Degrees (GEDs), and meet other benchmarks as they move to self-sufficiency. These two projects highlight the successful local strategies for involving faith-based and community organizations in affordable housing plans and promoting homeownership throughout the nation.

Other Support Offices

In addition to the program offices described above, HUD has the following support organizations.

The Office of Administration

http://www.hud.gov/offices/adm/

The Office of Administration is responsible for developing and implementing policies and procedures associated with human capital management and the administrative management of the Department. The Assistant Secretary for Administration advises the Secretary and senior management on administrative management and human resource matters.

The Office of the Chief Financial Officer

http://www.hud.gov/offices/cfo/

The Office of the CFO ensures that the Department employs sound financial management practices to help meet the Department's mission to promote adequate and affordable housing, economic opportunity, and a suitable living environment free from discrimination.

CFO staff functions include: accounting, budget, and financial management for HUD's budget appropriation. In addition, CFO financial systems process millions of transactions annually to support HUD projects and meet the needs of the housing community.

The Office of the Chief Information Officer

http://www.hud.gov/offices/cio/

The Office of the Chief Information Officer provides leadership, vision, and advice to the Secretary and other HUD senior managers on the strategic use of information technology to support core business processes and to achieve mission-critical goals by providing high-quality information technology solutions and services.

The Office of the Chief Procurement Officer

http://www.hud.gov/offices/cpo/

The Office of the Chief Procurement Officer awards and administers contracts and purchase orders, and provides vital procurement services to HUD's program and support offices.

The Office of Field Policy and Management

http://www.hud.gov/offices/fpm/

The Office of Field Policy and Management (FPM) provides direction and oversight for Regional and Field Office Directors. It communicates priorities and policies of the Secretary to these managers and ensures the effective pursuit of the Secretary's initiatives and special projects. It also communicates other management and administrative functions to the local field offices. In addition, the Office ensures that critical field program delivery issues are addressed and program impacts and customer service at the local level are assessed. The Office provides operational feedback designed to constructively influence program design and Departmental policy making.

FPM directs and coordinates the execution of the field offices' response (personnel and government operations) to natural and other types of disasters. Furthermore, FPM is the coordinating entity that oversees the Department's field offices and maintains plans for transfer of power and reconstitution, so as to allocate human capital and alternate facilities for required interoperable communications and essential functions within the field offices.

The Office of Congressional and Intergovernmental Relations

http://www.hud.gov/offices/cir/

The Office of Congressional and Intergovernmental Relations is responsible for coordinating Congressional and intergovernmental relations activities involving program offices to ensure the effective and accurate presentation of the Department's views. The Office also is responsible for coordinating the presentation of the Department's legislative and budget program to the Congress. It also monitors and responds to the HUD-related activities of the Department's Congressional oversight, authorizing, and appropriations committees.

The Office of Departmental Operations and Coordination

http://www.hud.gov/directory/dirodoc.cfm

The Office of Departmental Operations and Coordination performs a broad range of cross-program functions that assist the Secretary and Deputy Secretary with HUD's continuing management improvement initiatives. The mission of the Office is to directly support the Departmental strategic goal to "embrace high standards of ethics, management, and accountability," and directly or indirectly support the remaining strategic goals to advance homeownership, affordable housing, stronger communities, fair housing, and participation of faith-based and community organizations.

The Office of General Counsel

http://www.hud.gov/offices/ogc/

The Office of General Counsel (OGC) plays a vital role in helping the Department accomplish its mission of assuring decent and affordable housing, enabling all Americans to achieve homeownership, providing resources for communities to build strong neighborhoods, preventing homelessness, and enforcing fair housing laws. OGC attorneys provide legal opinions, advice and services with respect to all departmental programs and activities.

The Office of Inspector General

http://www.hud.gov/offices/oig/

The Office of Inspector General's mission is independent and objective reporting to the Secretary and the Congress for the purpose of bringing about positive change in the integrity, efficiency, and effectiveness of HUD operations.

The Office of Policy Development and Research

http://www.huduser.org/

The Office of Policy Development and Research is responsible for maintaining current information on housing needs, market conditions, and existing programs, as well as conducting research on priority housing and community development issues. The Office provides reliable and objective program evaluation, data, and analysis to inform policy decisions and improve program results. The Office is committed to involving a greater diversity of perspectives and methods in its research.

The Office of Public Affairs

http://www.hud.gov/news/index.cfm

The Office of Public Affairs works closely with local and national news media, as well as HUD program and policy contacts, to demonstrate to the public what HUD is doing for them and their communities.

RISKS, TRENDS, AND FACTORS AFFECTING GOALS

HUD operates under an annual budget that represents 1.2 percent of the federal budget[1] and 0.2 percent of the nation's $14.3 trillion gross domestic product. Within the housing market, HUD's FY 2008 budget amounted to 7.0 percent of the $503 billion invested into housing.[2] These comparatively small federal investments indicate that external factors strongly affect HUD's accomplishments and extend beyond its span of control. Understanding external factors enables more successful programs by allowing HUD to plan for contingencies, form strategic partnerships, and better focus and leverage resources to accomplish its strategic goals.

This section discusses the risks, developing trends, and factors that affect HUD's strategic goals in homeownership, rental housing, equal opportunity housing, community development, and HUD's management operations. This section is organized by three categories of external factors -- economic, demographic and social, and physical environment -- plus internal organization and management. Each subsection also summarizes key policy and program initiatives by which HUD is responding to the external factors.

Economic Factors

Mortgage and Financial Markets

In FY 2008, a national subprime mortgage crisis not only threatened HUD's goals of raising minority and low-income homeownership, but triggered a global financial crisis. The crises have led to record-level foreclosures and defaults, communities in decline, and an unstable housing market. Many homeowners that held subprime adjustable rate mortgages (ARMs) unexpectedly but inevitably faced interest rate shocks after their periods of low fixed rates ended. As a result, mortgage default rates, which were at record lows a few years ago, have increased sharply. In the second quarter of calendar 2008, 4.58 percent of all mortgages were in default or foreclosure, up from 3.30 percent a year earlier. Among subprime ARM mortgagors, 26.96 percent were in default or foreclosure in the second quarter, compared with 12.46 percent a year earlier.

Concentrated foreclosures have left many communities distressed as they exacerbate the decline of home prices and cause rising levels of abandoned or vacant properties. This has critical impacts on minorities and low-income households who committed to a major share of subprime mortgages.

The weakened housing market--along with uncertainty about risks associated with subprime loans, mortgage-backed securities and their derivatives in the capital market -- has led lenders to tighten mortgage credit. The most recent available data from the Home Mortgage Disclosure Act reporting show that 15.9 percent of mortgage applications were denied in 2007, the same as in 2006, but up from 13.8 percent in 2005. Higher denial rates, in combination with stagnant or declining prices, have blocked many homeowners' intended strategies to refinance ARMs before their higher rates kicked in.

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[1] FY 2007 budget authority, from "Budget of the U.S. Government, Fiscal Year 2009: Historical Tables," Table 5.2.
[2] Residential fixed investment. This and remaining statistics reported in this section, unless otherwise noted, are drawn from "U.S. Housing Market Conditions, 2nd Quarter, 2008," available at http://www.huduser.org/periodicals/ushmc.html.

Policy Response to Mortgage & Financial Markets

During FY 2008, the stabilization of capital markets became an area of intense focus for Congress, the Department of Treasury, and the Federal Reserve. Ongoing availability of credit is an issue with global reach, and is an essential precondition for stabilization of housing prices and default rates. It also has the potential for affecting HUD's goals in other ways, as tightened credit could trigger a broader economic downturn and reduce the ability of state and local governments to finance capital projects at reasonable cost.

HUD has responded to the direct housing aspects of the subprime mortgage crisis in a number of ways. These include developing and implementing program responses, including key components of the Housing and Economic Recovery Act (HERA) of 2008.

The **Federal Housing Administration** has improved its management practices and business processes to provide FHA insurance to more low-income households seeking to become homeowners or to secure homeownership for the future. FHA's efforts to modernize and streamline its business practices, and the recent FHA modernization bill, reflect HUD's emphasis on improving products, reducing risk, and automating business processes. In FY 2008, FHA expanded both the use of the Technology Open To Approved Lenders (TOTAL) scorecard and the eligibility standard for automated underwriting approval. This will result in direct savings to homebuyers and will expedite loan origination for thousands of households. The capital ratio for the FHA Mutual Mortgage Insurance Fund remains above the statutory minimum of 2 percent, even in the midst of the deepest housing recession of the modern era. That ratio was estimated by an independent actuarial study to be 3 percent at the end of FY 2008. The ratio represents reserves over-and-above what will be necessary to pay for expected insurance claims in the future. The capital ratio directly influences FHA's ability to continue to offer insurance coverage to mortgagors. It is vital in the current market environment that FHA be a viable option for homebuyers and for homeowners who need to refinance out of costly subprime mortgages. FHA's share of mortgage originations rose from under 2 percent in early 2007 to 22 percent in July 2008.

Early in FY 2008, HUD and the Department of Treasury encouraged mortgage market participants to form the HOPE NOW Alliance, including counselors, servicers, investors, and other groups. The Alliance provides coordinated outreach to homeowners in distress to help them stay in their homes. HUD-funded counseling organizations play a central role, providing borrowers with in-depth counseling about debt management, credit, and foreclosure prevention. The Alliance estimates that the efforts of the mortgage lending industry during the first three quarters of calendar 2008 had enabled approximately 1.6 million homeowners to avoid foreclosure.[3]

HUD also introduced *FHASecure* at the end of FY 2007 in response to the growing foreclosure crisis. *FHASecure* is helping homeowners with subprime ARMs refinance to affordable, fixed-rate, FHA-insured loans. Since inception, FHA assisted almost 369,000 homeowners through the *FHASecure* initiative as of September 30, 2008.

FHA default rates have been very stable while those for Subprime ARMs have escalated. FHA's seriously delinquent rate (defaults plus in-foreclosure) in the second quarter of FY 2008 was

[3] http://www.hopenow.com/media/press_release.php

5.43 percent, compared with 18 percent for all subprime loans, and 27 percent for Subprime ARM loans. Additionally, FHA has significant program safeguards that reduce and contain the risk of foreclosure for borrowers who experience mortgage default.

FHA also has taken substantial steps to reduce predatory lending among minority households and neighborhoods. This includes denying FHA insurance for mortgages on homes that have been "flipped" at inflated prices and deploying special monitors to pursue unscrupulous appraisers and lenders.

The **Housing and Economic Recovery Act**[4] has enabled FHA to better assist in the refinance of at-risk mortgages by establishing a $300 billion HOPE for Homeowners program. Through the Program, FHA helps distressed homeowners avoid foreclosure by insuring new, refinanced mortgages that have lower balances, fixed interest rates, and at least 30-year terms. To balance risk to the HOPE Insurance Fund, loans must be restructured so that mortgage payments are no more than 31 percent of monthly income, with an exception to 38 percent if the borrower first demonstrates the willingness and ability to make those higher payments. Also, all second mortgages must be canceled and all late fees and prepayment penalties must be waived. Mortgagees also must write down the loan's principal balance to 90 percent of the home's appraised value. This saves them from potentially larger losses should they rather pursue foreclosure, while at the same time creating a more stable situation for the homeowner.

The housing government-sponsored enterprises, Fannie Mae and Freddie Mac, were placed under conservatorship in September 2008, because they held inadequate reserves of capital relative to their probable risk from defaults. Through the HERA, Congress created the new Federal Housing Finance Agency, and transferred to it two key regulatory roles for the enterprises -- the safety and soundness oversight role of the Office of Federal Housing Enterprise Oversight, as well as HUD's role of regulating the enterprises' affordable housing mission. The conservatorship will allow the GSEs to remain liquid enough to inject needed capital to help steady the mortgage market.

Ginnie Mae also continues to guarantee mortgage-backed securities backed by federally insured or guaranteed loans. Ginnie Mae guaranteed $220.6 billion in securities during FY 2008, providing continued support for the secondary mortgage market while increasing market share. The twelve Federal Home Loan Banks, which also are government-sponsored enterprises, likewise continue to provide large amounts of mortgage capital.

Housing Supply and Prices

The nation's housing stock grew by 1.7 percent through the second quarter of 2008, adding a half-million each of owner- and renter-occupied units as well as more that 1.25 million vacant units. The rental vacancy rate of 10.0 percent in the second quarter was up from 9.5 percent a year earlier. Although rental vacancy rates remain above historical averages, many local rental markets have very little housing that extremely low-income renters can afford without HUD program assistance. Newly constructed apartments tend not to be affordable: those completed in the first quarter of 2008 had median asking rent of $1,111, up 16 percent from a year earlier.

Among single family homes, declining home prices (largely attributed to the mortgage crisis), and additions to the housing stock have made homeownership slightly more affordable in

[4] Public Law 110-289, available at http://www.gpoaccess.gov/plaws/index.html.

FY 2008, after a decade of rising home prices. In September 2008, the median sales price of an existing home was 8.8 percent less than a year ago. This was partially due to a more restrictive credit market and a drop-off of investor purchases that reduced demand for new homes. As a result, sales of new homes in September were 33.1 percent below last year's volume. Sales of existing homes, however, began to recover, with 7.8 percent more homes sold in September compared with a year earlier, and with the inventory of existing homes for sale shrinking by 2.4 percent over the same period.[5]

To reduce the surplus of new single-family homes, developers continued to slow construction of single family homes in FY 2008, after record level activity during 2005 and 2006. Seasonally adjusted annual rates for single family building permits during the second quarter of 2008 were 40 percent lower than a year earlier.

Household Incomes and Affordability

Affordable rental housing remains a challenging issue for the U.S. The most recent data show that in 2005, 5.99 million very low-income renter households had "worst case needs," either by having severe rent burdens (91 percent), severely inadequate units (4.4 percent), or both (4.3 percent).[6] This was primarily due to the insufficient supply of rental units affordable to households with extremely low-incomes.

However, the "housing opportunity index," (HOI) calculated by the National Association of Home Builders and Wells Fargo showed an improvement in housing affordability for single family owner-occupied homes. HOI represents the percentage of homes that are affordable to a median income family in a metro area. The index improved to 55.0 percent in the second quarter of 2008, a jump of 11.9 points from a year earlier, and implying that over half of homes sold were affordable to median income families. Nevertheless, the index value of 63.7 percent recorded in 2002 and 2003 was substantially better, because both home prices and interest rates were lower then.

As a result, homeownership remains out of reach for many low and moderate income families. Given the nation's record level foreclosures and defaults, the demand for affordable rental housing is likely to increase further. However, limited federal resources for housing assistance constrain HUD's ability to provide access to more affordable housing. Substantial increases in voucher costs and utilization have strained HUD's Section 8 program resources.

Residential energy costs are often overlooked as a factor affecting housing affordability. According to the Joint Center for Housing Studies, 2.5 million extremely low-income households spent more than 30 percent of their incomes on home energy in 2003.[7] From the end of 2002 to September 2008, housing "fuels and utilities" prices have increased by 58 percent.[8] High energy prices pose a risk to HUD's public housing and Section 8 programs, which cover utility costs as part of gross rents.

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[5] Figures are seasonally adjusted annual rates. New home sales and median prices are reported by the Census Bureau at http://www.census.gov/const/www/newressalesindex.html, and existing home sales and median prices are reported by the National Association of Realtors at http://www.realtor.org/research.nsf/Pages/EHSdata .

[6] HUD, 2007, "Affordable Housing Needs 2005: Report to Congress." http://www.huduser.org/publications/affhsg/affhsgneeds.html

[7] Joint Center for Housing Studies of Harvard University, "The State of the Nation's Housing 2006," page 8.

[8] See Consumer Price Index tables for urban consumers at http://www.bls.gov/cpi/#tables.

Employment

The **unemployment rate** is an indication of shocks to household income that may make housing unaffordable. Due to a waning economy and an unstable housing market, the unemployment rate increased to 6.1 percent at the end of FY 2008, up from 4.7 percent a year earlier. According to the Bureau of Labor Statistics, FY 2008 closed with a net loss of 519,000 jobs, following gains in the first quarter.[9] The industries with the greatest numbers of unemployed persons are construction, manufacturing, and professional business services. The manufacturing sector currently accounts for 9.7 percent of total non-farm employment, but is expected to shrink to 8.2 percent by 2014. Communities that continue to rely on manufacturing employment may be adversely affected by this trend, although such losses sometimes are compensated by economic transformation and gains in new skills accrued by manufactured workers. These macroeconomic trends can affect HUD's success in strengthening communities.

At the local level, unemployment can indicate workforce skill gaps, or spatial mismatches between unemployed workers and available jobs that are exacerbated by insufficient transportation options. Many older communities also face fiscal pressures as they struggle to provide quality services, attract employers, and manage the deterioration of housing stock, especially as real estate values decline eroding the property tax base. Rural communities often face additional challenges because of the changing structure of the farming industry, under-investment, weak infrastructure, limited services, and few community institutions.

For individuals in marginal housing situations or challenged by personal issues, loss of employment can quickly lead to homelessness**.** Along with the availability of low-cost housing, personal issues such as domestic violence, substance abuse, mental illness, disabilities, and lack of education and job skills can lead one to become homeless.

Policy Responses to Other Economic Factors

Federal budget constraints have made it challenging to expand the nation's affordable housing supply. In recent years, federal expenditures for production of rental housing largely have been through the Low Income Housing Tax Credit. With $5 billion of annual budget authority, the tax credit program, in combination with HUD programs such as HOME and CDBG, adds more than 100,000 units annually, of which 95 percent qualify as affordable.[10]

The Housing and Economic Recovery Act provided $3.92 billion of emergency assistance grants under CDBG to stabilize communities that have been harmed by concentrated foreclosures. The ***Neighborhood Stabilization Program*** grants may be used to acquire and redevelop foreclosed properties that otherwise would trigger further abandonment and blight. HUD allocated the funds at the end of FY 2008, for communities to use within 18 months.

Resource constraints, especially for rental housing, have led HUD to improve its verification of tenant income for households receiving rental assistance to ensure the efficient and fair allocation of resources. Tenant-paid rents are established as a percentage of income in HUD's rental assistance programs, so that lower tenant incomes require larger rent subsidies. The

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[9] From the table "Employment, Hours, and Earnings from the Current Employment Statistics survey (National)," at http://www.bls.gov/data/#employment. August and September estimates remain preliminary as of Oct.10, 2008.

[10] Office of Policy Development and Research (January 2006), "Updating the Low Income Housing Tax Credit Database: Projects Placed in Service Through 2003," available athttp://www.huduser.org/Datasets/lihtc/report9503.pdf

Department has worked to ensure that tenants do not under-report wages, social security benefits, and unemployment income and that assisted housing providers adequately verify reported income.[11] HUD has cooperated with program partners and tenant groups to strengthen and adhere to internal controls. In FY 2006, HUD implemented the Enterprise Income Verification system (EIV) to enable housing agencies to more accurately verify tenant income. The expansion of the verification process to assisted multifamily programs[12] in FY 2008 will eliminate the majority of improper payments attributable to tenant underreporting of income. This effort might also be strengthened by statutory changes to simplify and standardize subsidy program requirements.

HUD also has implemented regulatory changes to the operating subsidy program to move public housing agencies toward asset management practices and greater energy efficiency. PHAs will be able to reduce operating costs, retain savings, and take advantage of financial incentives and strategies for reducing utility consumption.

Regulations also provide for Energy Performance Contracts to help PHAs control utility and maintenance costs. These contracts are part of an innovative financing technique that uses cost savings from reduced energy consumption to repay the cost of energy conservation measures. The Federal Energy Policy Act of 2005 enhanced the contracts by extending payback periods from 12 to 20 years. This flexibility makes the contracts financially more attractive to small and medium size PHAs, and can generate funding to incorporate more energy-saving retrofits.

To improve energy efficiency among homeowners, FHA is offering energy efficient mortgages to homebuyers and homeowners that seek to upgrade their homes to reduce energy consumption. In addition, HUD has partnered with the Department of Energy to promote the use of Energy Star products within HUD programs, including in housing developments financed by HOPE VI, HOME, and CDBG.

Demographic/Social Factors

Demographic factors, such as growing populations of seniors and persons with disabilities, also affect HUD's strategic goals. The elderly population (65 and older) is projected to increase from 12 percent in 2000 to 19 percent by 2030, with rapid growth beginning in 2010. As life expectancy continues to lengthen, helping the elderly to remain homeowners or age in place will become increasingly important for containing medical costs and improving quality of life.

For persons with disabilities, the Supreme Court in 1999 ruled that states must place persons with disabilities in community settings rather than institutions when treatment professionals determine that community placement is appropriate (Olmstead vs L.C. (98-536) 527 U.S. 581 (1999)). As a result of this decision, more persons with disabilities could be moving into communities where the supply of affordable housing remains low. Local resistance to group housing, along with zoning regulations, frequently become barriers to meeting the housing needs of this disadvantaged population.

Another demographic trend is the growth of the Hispanic population. This ethnic shift, projected to reach 23 percent of the population by 2030, will continue to create new and evolving

[11] For more information, please see "Improper Payments" discussion in Section 4 of this report.
[12] See http://www.hud.gov/offices/adm/hudclips/notices/hsg/files/08-03HSGN.doc

challenges for HUD's fair housing responsibilities, for rental housing and homeownership, including housing counseling, and for community development, including the Colonias.

Geography of Poverty

The past decade has seen significant changes in the distribution of poverty within numerous U.S. metropolitan areas. HOPE VI redevelopment and expanded use of vouchers has dispersed large concentrations of poverty associated with large public housing developments. In parallel with this trend, mixed income communities and upscale loft housing development are reviving 24-hour city living in urban cores.

However, gentrification, such as sometimes occurs when older affordable neighborhoods experience rapid increases in demand, has had negative side effects by displacing low-income households to suburban areas. Between 1999 and 2005, growth in the numbers of suburban poor outpaced growth of poor persons in central cities by 1 million people.[13] This trend may continue as cities face declines in affordable housing stock, rising home prices, and continued gentrification of poorer neighborhoods. The quality of neighborhood schools interacts strongly with poverty and neighborhood quality. Countless families with children make location decisions based on schools, leading frequently to neighborhoods sorted by income.

Public Awareness of Fair Housing Law

HUD's survey, the Housing Discrimination Study 2006, revealed the need for greater education on some aspects of the fair housing laws.[14] The most recent work indicates that the public has become more aware of protections for families with children and prohibitions of racial steering, but was less aware of laws that prohibit advertisements that discriminate on the basis of religion. The lack of public awareness of housing discrimination laws greatly hinders HUD's ability to enforce fair housing, affecting both compliance and responses of victims. Other HUD studies have found persistent discrimination against African Americans, Hispanics, Asians, and Pacific Islanders in residential sales and rental markets. HUD's research also has revealed discrimination against persons with disabilities, including frequent refusals to allow reasonable accommodations.

While HUD's studies suggest that housing discrimination occurs frequently, victims do not always report the discrimination. This may be due to a tenant's lack of education regarding the fair housing law or the erroneous belief that filing a compliant would cost them money. HUD's public awareness study found that 90 percent of persons who experienced housing discrimination did nothing; and one percent reported that they filed a complaint with a government agency.

Policy Responses to Demographic Factors

To assist elderly populations in affordable homeownership, FHA's Home Equity Conversion Mortgage program endorsed 111,661 reverse mortgages in FY 2008, raising the total since the program's inception to 454,745 loans. These reverse mortgages support aging in place and adequate incomes for elderly homeowners by allowing them to tap into home equity.

[13] Brookings Institute. "Two Steps Back: City and Suburban Poverty Trends 1999–2005." http://www.brookings.edu/reports/2006/12poverty_berube.aspx
[14] Available at www.huduser.org

To enhance the private response to housing needs for persons with disabilities, HUD works with teams to help improve the International Building Code and the International Residential Code. The cooperative effort periodically updates the codes to ensure that multifamily housing developers comply with statutory accessibility requirements that meet the needs of disabled populations.

Community needs and urban conditions and challenges have evolved substantially over the past several decades. To address these challenges, including those related to shifting demographics, HUD has proposed Community Development Block Grant reform. The legislation would reform the CDBG allocation formula to more equitably target funds toward current community needs and to promote more focused efforts within jurisdictions. HUD also continues to strengthen the use of performance measurement for community development.

To reduce housing discrimination, HUD continues to promote fair housing by investigating, conciliating, and prosecuting discrimination in the private market, and ensuring non-discrimination in its own programs. The Department is reviewing regulatory requirements and responses concerning "analyses of impediments" to fair housing that jurisdictions conduct as part of their planning for community development. Additionally, FHA has worked to ensure equal housing opportunities through targeted marketing and outreach to unserved and underserved markets.

Physical Environment Factors

Natural disasters have provided ongoing challenges and risks to many of HUD's strategic goals, destroying lives, infrastructure and housing stock, and displacing families. In 2005, hurricanes Katrina, Rita and Wilma severely damaged or destroyed an estimated 193,000 owner-occupied homes,[15] of which many were occupied by families with low- or very low-incomes. Similar dangerous and destructive hurricanes continued to occur in 2008, while severe thunderstorms brought a "500-year" flood to Iowa and other states. Evidence that severe hurricane activity may worsen highlights the risk of extensive development of coastal areas in recent decades. Additionally, disasters such as severe earthquakes and wildfires along the West Coast or the Midwest's New Madrid fault could radically reshape urban America, as could further terrorist actions.

Land Use and Development

Rising land costs, congestion, and local zoning ordinances are among the factors affecting private decisions about residential location as well as commercial development. As the price of land increases, private developers may choose to construct less affordable single and multifamily housing without additional federal assistance. Because affordable units for rent and sale are priced below the market rate, private developers may produce less affordable units if their construction costs are too high.

Local zoning ordinances and land use controls can prevent the construction of affordable housing. Land use policies that require minimum density or lot sizes can indirectly affect construction costs and the types of housing built. High housing prices may force lower income households away from their place of employment to areas where housing is more affordable.

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[15] "Current Housing Unit Damage Estimates: Hurricanes Katrina, Rita and Wilma, February 12, 2006," available at http://www.huduser.org/Publications/pdf/GulfCoast_HsngDmgEst.pdf

This has increased traffic congestion and average commuting times, and high commuting costs are exacerbated by recent increases in fuel prices.

Policy Responses to Physical Environment Factors

While much of the federal initiative to assist hurricane efforts remains with the Federal Emergency Management Agency (FEMA), HUD received a mission assignment from FEMA to assist with re-housing families displaced from the Gulf Coast. FHA's loss mitigation solutions enabled more than 20,000 homeowners in areas afflicted by Katrina, Rita, and Wilma to retain homeownership through the end of FY 2008. HUD has marshaled a full range of program authority in the service of rebuilding New Orleans and other hurricane-damaged communities. HUD has allocated more than $19 billion in CDBG disaster supplemental grants to the Gulf Coast states where 90 percent of funds have been used for housing-related activities. This includes the resident relocation, housing rehabilitation and development reconstruction. Additionally, improved coordination with FEMA in disaster response planning will pay dividends in future disasters.

Although land use remains primarily a state and local issue, HUD is addressing land use costs in the form of regulatory barriers through a focused research program and sharing of best practices. The Regulatory Barriers Clearinghouse provides an extensive array of strategies intended to support affordable housing. Additionally, HUD is engaged with the Federal Transit Administration to promote affordable housing near transit through the coordination of housing and transportation programs.

Organization and Management Factors

In addition to the three categories of external factors identified above, several additional types of factors affecting performance and risk are tied more directly to internal processes and organization. These factors and HUD's responses are discussed here.

Relations with Business Partners

Communities have a great deal of flexibility when using HUD funds to address economic conditions. Local partners can use several programs, and particularly CDBG, for a variety of eligible activities such as job training and small business development. However, this local discretion complicates HUD's ability to set goals and assess results at a national level. HUD is working closely with state and local partners to enhance local assessments without restricting CDBG flexibility.

Additionally, program success requires active participation from a wide variety of organizations. For example, the continuum of care needed to assist homeless populations engages a wide variety of partners, which may include state and local agencies, nonprofit organizations, service providers, housing developers, private foundations, the banking community and local businesses. Increasing fiscal constraints of state and local governments may reduce their ability to contribute to shared objectives.

Federal Workforce

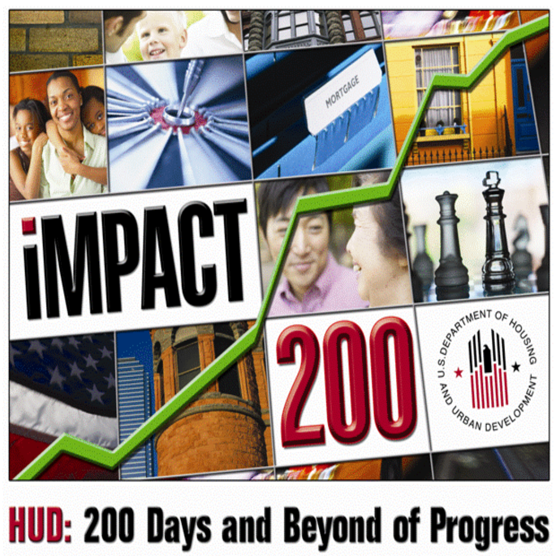
Like many federal agencies, HUD has an aging workforce, where more than 58 percent of employees are eligible to retire within the next three years. Succession planning is critical, yet workforce planning is hindered by lack of funding to support authorized full-time equivalent staffing levels. The funding gap is worsened by the need to fund salary increases that are not provided in HUD's annual appropriations. To use funds more effectively, HUD is using a variety of tools including employee surveys, workforce planning, and a centralized training strategy to upgrade staff capabilities.

To ensure continued program accountability under staffing constraints, HUD is refining and strengthening the use of risk-based techniques for monitoring programs. When monitoring reveals significant performance and compliance problems, HUD must act appropriately to address those problems to minimize the risk and advance program objectives.

Information Management

Adequate funding of HUD's information technology portfolio is necessary in efficiently managing HUD programs. Funding constraints have hindered progress in upgrading outdated legacy systems that support critical program operations and financial controls. HUD needs the commitment and funding to complete the modernization of legacy information systems, employing enterprise architecture principles. HUD also has established a collaborative structure through which HUD program managers assume a stronger system ownership role in assuring that systems requirements and controls over data quality and security are properly established. These efforts will result in improved program delivery and better support for HUD's mission.

The Secretary's Management Agenda



Secretary Preston assumed the leadership of HUD in June 2008. Upon his confirmation, the Secretary embarked on an ambitious agenda to further enhance HUD's performance and advance HUD's mission. This agenda -- entitled *iMPACT 200* -- provides a framework for his term of roughly 200 days as Secretary of the Department. It focuses on ways to support our constituents, provide transparency to our major initiatives, and move the Department forward. *iMPACT 200* is built on the idea that HUD must engage its customers and empower its employees. At a time when HUD's mission has never been more important, *iMPACT 200* establishes reasonable timetables and relies on the outstanding service, personal sacrifice, and total commitment of the HUD team to accomplish three strategic goals:

- Promote responsible, sustainable homeownership for all Americans,
- Maximize options for safe and affordable housing so all Americans can embark on a path to self-sufficiency, and
- Deliver effective, timely service to our customers, employees, and partners.

The Department has made significant progress on the Secretary's agenda. Of major significance is the implementation of the new housing legislation, the Housing and Economic Recovery Act of 2008, which established the *HOPE for Homeowners* and *Neighborhood Stabilization*

Programs. The Act also expanded authority for the *FHASecure* program that had already assisted over 368,000 homeowners since its inception in 2007.

Additionally, the Department has also undertaken several Business Process Reengineering (BPR) efforts in the Offices of Housing, Administration, and Procurement as part of the Secretary's agenda. The Office of Housing has led the way on Lean BPRs with an initiative to accelerate automation and streamlining across all FHA program areas. This same Lean BPR technique is being applied by the Office of Administration to improve the Human Resources function and streamline the process for recruitment and hiring new employees, while providing a blueprint of the BPR staffing/hiring process to the incoming Administration. The Office of the Chief Procurement Office also is undertaking a Lean BPR effort to strengthen and improve the procurement and acquisition process by mapping and automating the current process from the annual strategic plan through award, creating paperless procurement request process, reducing the number of forms significantly, standardizing the review process, and providing improved accountability.

President's Management Agenda

In FY 2002, the Office of Management and Budget (OMB) published the President's Management Agenda (PMA), as set forth by President George W. Bush, to implement government reform that is citizen-centered, results-oriented, and market-based. The Secretary and Deputy Secretary have emphasized, and HUD's Strategic and Annual Performance Plans reflect, activities designed to achieve the outcome goals of the PMA.

During FY 2008, these initiatives included (Year initiated):

- Strategic Management of Human Capital (FY 2002),
- Commercial Services Management (formerly Competitive Sourcing) (FY 2002),
- Improved Financial Performance (FY 2002),
- Expanded Electronic Government (FY 2002),
- Performance Improvement (FY 2002),
- Increased Faith-Based and Community Organization Participation (FY 2003),
- Eliminate Improper Payments (FY 2005), and
- Credit Program Management (FY 2006).

While the first five of these initiatives are government-wide, the last three were identified by OMB and HUD officials as significant areas for improved performance at the agency level. A fourth HUD-specific Initiative entitled "Improved HUD Management and Performance" was established in FY 2002, and the actions associated with this Initiative were successfully completed in FY 2007, resulting in HUD receiving a final rating of GREEN and removal of this Initiative from the PMA. This HUD-specific performance indicator was primarily established to address GAO-designated high-risk program areas and material internal control weaknesses not addressed by the other initiatives of the PMA.

In order to ensure that the management orientation at HUD remains deeply committed to achieving PMA goals, the Secretary and Deputy Secretary have instituted the following activities to ingrain the PMA into HUD's normal management processes:

- Incorporated PMA goals in the Department's Strategic, Annual Performance, and Management Plans;
- Assigned Assistant Secretaries or equivalent level positions as PMA Initiative Owners with responsibility for planning, coordinating, and acting to achieve PMA goals;
- Developed an annual plan of actions and milestones to reflect where HUD would be "Proud-To-Be" on PMA goals, with quarterly refinements in discussion with OMB;
- Held quarterly meetings with OMB to review and discuss their quarterly scorecards on the status of overall goals and quarterly progress in completing the planned actions; and

- Communicated PMA criteria, plans, progress, and accomplishments to HUD staff and interested parties through print media, the HUD web site, and satellite broadcasts.

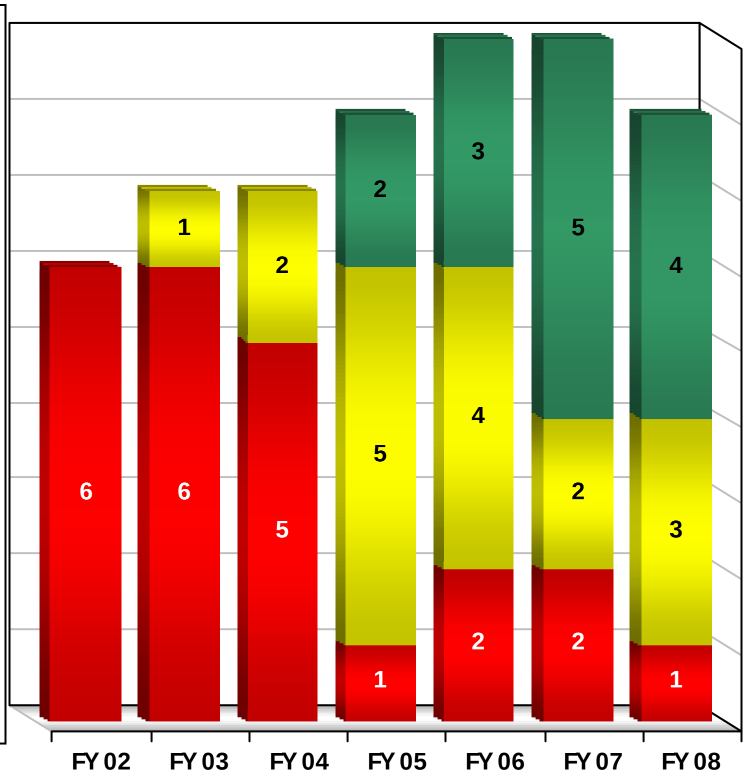
Following is a summary table followed by a detailed description of HUD's FY 2008 PMA activities and results as of June 30, 2008:

OMB instituted a "stoplight" scoring system to evaluate the status and progress of each agency.

- **Green** for success,
- **Yellow** for mixed results, and
- **Red** for unsatisfactory.

Status:
At end of the first reporting cycle in June of FY 2002, most agencies, including HUD, were evaluated as mostly RED. Since that time, HUD has made steady progress in striving for GREEN status for all its initiatives.

As of the reporting cycle ending June 30, 2008, HUD earned four GREEN scores, three YELLOW, and one RED status score.

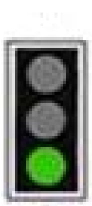


HUD's Overall PMA Scoring Progress 2002-2008

↑↓ Denotes an increase (decrease) in the status score from the previous year.

Initiative	HUD's Overall PMA Scoring Progress 2002-2008 By Initiative						
	June 2002	**June 2003**	**June 2004**	**June 2005**	**June 2006**	**June 2007**	**June 2008**
Human Capital	Red	Red	↑ Yellow	Yellow	Yellow	Yellow	↑ Green
Commercial Services/ Competitive Sourcing	Red	Red	Red	↑ Yellow	Yellow	↓ Red	↑ Yellow
Improved Financial Performance	Red	Red	Red	Red	Red	↑ Green	Green
Expanded E-Government	Red	Red	Red	↑ Yellow	↑ Green	Green	↓ Yellow
Performance Improvement	Red	Red	Red	↑ Yellow	Yellow	Yellow	Yellow
HUD Management and Performance	Red	Red	Red	↑ Yellow	Yellow	↑ Green	Complete*
Faith-Based and Community Initiatives	N/A	Yellow	Yellow	↑ Green	Green	Green	Green
Eliminate Improper Payments	N/A	N/A	N/A	↑ Green	Green	Green	Green
Credit Program Management	N/A	N/A	N/A	N/A	Red	Red	Red

* Management and Performance. The actions associated with the Management and Performance initiative were successfully completed, and HUD received a final rating of GREEN.

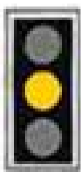


1. Human Capital. HUD has received a rating of GREEN for status and GREEN for progress for this initiative. HUD's Human Capital initiative is structured to accomplish the PMA goal of having processes in place that ensure quality personnel are selected and performing at optimum levels. The Department continues to demonstrate that, like the majority of agencies, the effective management of human capital is fast becoming one of HUD's most pressing needs. The Department continues to focus on the core tenets of the President's Management Agenda initiatives, which seek to ensure:

1) Optimization of HUD's organizational structure; 2) implementation of succession strategies to assure a continually-updated talent pool; 3) performance appraisal plans for managers and staff adhere to merit system principles, enabling accountability for results while linking the goals and objectives of HUD's mission; 4) sustaining the established processes that address diversified hiring practices; 5) continued reduction of mission critical skill gaps; and 6) that corrective actions will be taken based upon developed human capital accountability systems.

To achieve the Green score on this Initiative in FY 2008, HUD:

- Demonstrated progress in reducing identified skill gaps and in continuing to pursue a more optimal organization;
- Developed a Succession Management Plan to address the potential retirement of approximately 60 percent of HUD's workforce over the next 3 years;
- Fully integrated its strategic and annual plan goals with the performance appraisal plans for all executives, managers, supervisors, and employees to promote a Department wide results-oriented performance culture.



2. Commercial Services Management. HUD has received a status rating of **YELLOW** and a **YELLOW** progress score for this initiative. Commercial Services Management is designed to ensure that the government acquires services at the best value for the taxpayer, regardless of whether the service provider is a public entity (government staff) or private entity (contractor staff). This initiative reflects the Government's commitment to find the most cost effective way to perform functions that are identified as potentially non-governmental, i.e., able to be performed by commercial entities without jeopardizing delivery of program services to citizens and HUD's clients. Commercial Services Management also tracks internal Business Process Reengineering (BPR) efforts pursued by HUD to improve its operations.

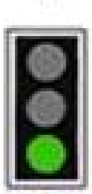
Prior to the President's emphasis on competitive sourcing, HUD had already outsourced many of its services, and accordingly it must carefully consider the affect on program risk of any further outsourcing. To date, the Department had completed seven competitions and implemented the results of five, with an anticipated cost savings totaling $22.6 million over a period of five years. However, no new competitions were held in FY 2008.

During FY 2008, HUD began implementation of the results of a streamlined competition announced last fiscal year on the Employee Service Center function within the Office of Administration that provides human resource management support.

The Department continues to explore opportunities for improving the efficiency with which we support our customers, and continued its BPR efforts on the Controlled Correspondence and IT Web functions. Additionally, the Department has undertaken Lean BPR reviews in the Offices of Housing, Administration, and Procurement. The Office of Housing has led the way on Lean BPRs with an initiative to accelerate automation and streamlining across all FHA program areas. To date, the Lean BPR approach has been used for the following two Housing programs:

- **232-223(f) Skilled Nursing Facility/Assisted Living Facility:**
  Project Charter: To improve consistency of decisions and processing and timeliness in reaching firm commitment and closing of 232 applications.
- **Single Family (SF) Home Ownership Center (HOC) endorsement process:**
  Project Charter: Improve process efficiency to maximize resources to handle the increased volume/demand, as well as to respond to crisis in the mortgage industry and prepare for the new legislation.

This same Lean BPR technique is being applied by the Office of Administration to improve the Human Resources function and streamline the process for recruitment and hiring new employees, while providing a blueprint of the BPR staffing/hiring process to the incoming Administration. The Office of the Chief Procurement Office also is undertaking a Lean BPR effort to strengthen and improve the procurement and acquisition process by mapping and automating the current process from the annual strategic plan through award, creating paperless procurement request process, reducing the number of forms significantly, standardizing the review process and providing improved accountability.



3. Improved Financial Performance. HUD is one of 13, out of a total of 26 major agencies, to earn a GREEN status and GREEN progress rating. Financial performance is a significant indicator of an agency's ability to fulfill its mission and meet the needs of the citizens and their government. Adequate control over financial operations enables the agency to reduce the risk of fraud, waste, and abuse; and provide support for informed budget and program decisions.

To these ends, the President has directed this initiative to: 1) Improve financial audit results; 2) Eliminate material weaknesses and strengthen internal controls; 3) Meet financial reporting deadlines; 4) Strengthen funds control and financial systems compliance; and 5) Improve the availability of financial data (dashboard reporting) needed to better inform budget and program decision-making.

During the year, HUD continued to maintain its status of GREEN based largely on:

- Achieving its ninth consecutive unqualified audit opinion on its consolidated financial statements;
- Eliminating its two FY 2007 auditor identified material weaknesses;
- Meeting all accelerated financial reporting requirements;
- Reducing unexpended funds balances to necessary levels;
- Implementing strengthened policies, procedures, training, and practices related to HUD's administrative control of funds;
- Achieving full compliance with OMB's A-123 assessment and assurance requirements for internal controls over financial reporting;
- Ensuring financial management systems are substantially compliant with FFMIA requirements; and
- Demonstrating effective uses of financial information to drive improved performance results through HUD's Financial Data-Mart, with plans for further continuous improvements.

Our progress and success have been recognized by our toughest examiners, the HUD Office of Inspector General, the GAO, and our OMB examiners.

4. Expanded Electronic Government. On June 30, 2007, HUD was one of five government agencies that had achieved GREEN status out of 26 agencies that were rated on this initiative. For each of the next three quarters, HUD continued to achieve GREEN status until June 30, 2008, when HUD's E-Government Initiative status score fell to **YELLOW.** The progress score also fell to **YELLOW** that quarter.

The President's E-Government initiative stresses the value of electronic methods for providing greater levels of public service at lower cost. HUD is a recognized leader among government agencies for this initiative.

Through the first three quarters of FY 2008, HUD met all the requirements for maintaining GREEN status based on actions that included:

- Implementation of an Enterprise Architecture that is guiding HUD's IT investment decisions in an efficient and effective manner;
- Progress towards completion of the E-Government Initiatives Implementation plan;
- Improvements to IT project management, with adherence to project cost, schedule and performance goals over 90 percent of the time;
- Maintenance of an approved NCS 3-10 plan for Continuation of Operations (COOP) and Continuation of Government (COG);
- Full compliance with the Federal Information Security Management Act (FISMA), as verified by the HUD OIG; and
- Completion of all reports, certifications, notices, and assurances in a timely fashion.

HUD was downgraded by OMB, however, for failure to fulfill all E-Government funding requirements and for failure to submit a revised Grants Management Line of Business Strategy Plan that comports to OMB's mandate. While HUD has worked extensively with Congress to obtain the necessary funding, certain funding requirements are still outstanding. HUD received a cut of 21 percent ($65 million) of its overall IT budget in FY 2008. Without the necessary appropriations, HUD was unable to proceed in the implementation of certain aspects of the E-Government implementation plan that require congressional funding.

HUD's E-Government performance has not gone unnoticed, however. HUD received the "2008 Excellence.Gov" Award from the American Council of Technology for implementation of the Enterprise Income Verification system that verifies income and benefits for low-income households, an important tool for eliminating improper payments. HUD also received the Intergovernmental Solutions Awards for development of the National Housing Locator System, now available to federal, state, and local agencies to rapidly identify available housing for citizens displaced from their homes by natural or man-made disasters. The system was developed in 2006 upon recognition of a need that became clear in the wake of hurricane Katrina. Currently, the National Housing Locator System identifies more than 350,000 rental housing vacancies available nationwide.

5. Performance Improvement Initiative. HUD has received a status rating of **YELLOW** and **GREEN** on progress for this initiative. The Performance Improvement Initiative -- which was formerly called the Budget and Performance Integration initiative of the PMA -- seeks to ensure that performance is routinely considered in funding and management decisions, and that HUD's programs achieve expected results and work toward continual improvement. Additionally, this initiative provides for clear, measurable program outcome goals and indicators to support budget and resource allocation decisions based on performance results. OMB developed this initiative and the associated Program Assessment Rating Tool (PART) to better validate that programs have clearly defined and measurable program outcomes, efficiency measures, and marginal cost measures to inform the budget decision-making process and improve performance.

HUD has maintained a status of YELLOW while working with OMB to complete 35 PART assessments covering all of HUD's major programs and nearly all of its annual budget authority. Of the programs assessed, OMB determined that 22, or 63 percent, were Effective, Moderately Effective, or Adequate. OMB rated the remaining13 programs, or 37 percent, as either Ineffective or Results Not Demonstrated.

The PART results have been used to help make decisions in the President's Budget request to the Congress. HUD continues to work with OMB to more clearly define expected outcomes for each of program and to produce better outcome and efficiency measures that evidence the programs are cost-effective and producing desired results.

Throughout FY 2008, HUD clearly demonstrated its ongoing efforts to achieve the goals set forth in the President's Management Agenda. To date, HUD has accomplished the following:

- The Department has reported important progress in key outcome areas including the initiation of the *FHASecure* program to improve homeownership and deal with the foreclosure crisis. This effort has been greatly expanded upon by the enactment of the Housing and Economic Recovery Act of 2008 that provides an even broader response to the homeownership and foreclosure issues that the Nation faces. The Department has made significant progress in developing more and better outcome measures, and in improving performance in programs that were previously scored as having Results Not Demonstrated under OMB's PART.

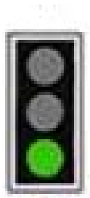
- A further significant accomplishment is the provision of disaster and emergency relief to areas impacted by hurricanes Katrina, Rita, Wilma and Ike and Gustav, as well as Midwest floods and other recent disasters.

- The Department named a Performance Improvement Officer to address improvement actions and future plans. Meetings are held on a regular basis by senior agency officials to review program and departmental performance.

- The Department established performance standards and plans for all levels of employees linked to the agency mission and strategic goals.

- For the second consecutive year, HUD received the Certificate of Excellence in Accountability Reporting (CEAR) award for its FY 2007 Performance and Accountability Report (PAR).

- The Department updated reporting on results through the ExpectMore.gov website, available to the public. Progress is noted on all major areas including the assisted affordable housing rental programs, community development programs, fair housing programs, and homeownership and other housing development and supportive programs.



6. Eliminate Improper Payments. The Department continues to be a leader in obtaining GREEN status and GREEN progress ratings for this initiative. This initiative implements the Improper Payments Information Act of 2002, which requires federal agencies to annually assess improper payment risks and to measure improper payment levels and report on progress in reducing those levels in programs and activities that may be susceptible to combined improper payments in excess of $10 million per year. The Act holds agency managers accountable for strengthening financial management controls in order to reduce any significant improper payment levels identified.

The specific objectives are to:

- Establish an annual agency-wide risk assessment process that identifies all programs at risk of significant improper payments;
- Provide for annual estimates of improper payment levels in at-risk programs;
- Analyze the causes of improper payments in at-risk programs to serve as the basis for setting reduction goals and corrective action plans; and
- Provide annual reporting of progress and results in attaining improper payment reduction goals.

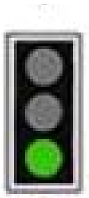
In FY 2005, HUD became the first agency to earn a GREEN status by reaching full compliance with the Improper Payments Information Act of 2002, and achieved the President's goals for eliminating improper payments. In FY 2008, HUD reduced improper payments by 71 percent from the FY 2000 baseline of $3.43 billion to FY 2007 results of $993 million. (There is a one-year lag in the reporting of improper payments.)

The overall reduction in improper payments for HUD's Rental Housing Assistance programs is primarily attributed to HUD's efforts to work with its housing industry partners through enhanced program guidance, training, oversight, and enforcement. Collectively, these efforts have had a positive impact on the program administrators' ability to reduce their errors in the calculation of income and rent.

In HUD's Public Housing program, significant program structure changes were implemented to improve the efficient use of funding in the Public Housing Operating Fund. These structure changes effectively eliminated improper payments in all three previously reported error sub-components – Administrator, Income Reporting, and Billing. In addition, the establishment of a budget based funding methodology in the Housing Choice Voucher Program eliminated the opportunity for billing errors.

The Department also has found a direct correlation in the reduction of improper payments to the number of monitoring reviews of public housing and the number of management and occupancy reviews of multifamily housing, as well as the expanded use of the Enterprise Income

Verification system to owners, management agents and contract administrators for HUD's Project Based Assistance programs.

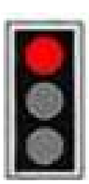


7. Increased Faith-Based and Community Organization Participation. HUD was the first of eleven agencies to earn a status rating of GREEN and continues to maintain its GREEN status. HUD also maintained a GREEN progress score on this initiative. These 11 agencies are leading the government-wide effort to promote participation of faith-based and other community organizations.

The Department's objectives for this initiative continue to include: reduce barriers to participation by faith-based and community organizations; conduct outreach and provide technical assistance to faith-based and community organizations to strengthen their capacity to attract partners and secure resources; and encourage partnerships between faith-based and community organizations and HUD's traditional grantees.

During FY 2008, HUD's Office of Faith-Based and Community Initiatives facilitated 68 grant writing seminars in 68 cities, began publishing monthly on-line newsletters for faith-based and community organizations, and conducted various technical assistance programs to maintain its GREEN status on this initiative. Additionally, HUD continued its efforts to:

- Identify and eliminate unnecessary regulatory and administrative barriers to faith-based participation;
- Improve data collection on faith-based participation;
- Initiate several successful pilot program efforts designed to better utilize faith-based organizations in HUD's program delivery -- such as the Unlocking Doors Initiative (UDI) which partners cities with faith-based and community organizations to improve their effectiveness in implementing affordable housing and homeownership strategies; and
- Encourage faith-based and community organizations to apply for HUD funding. From FY 2006 to FY 2007, the number of grants to these organizations increased from 1,160 to 1,226, an increase of 5.3 percent. (FY 2008 data is not yet available.)



8. Credit Program Management. HUD received a RED status rating and a GREEN progress rating for progress for this new initiative. This initiative addresses the effectiveness of direct and guaranteed loan programs to ensure that HUD's credit programs are reaching the targeted borrowers at an acceptable, manageable risk level. Credit Program Management is applicable to the five largest credit agencies (Agriculture, Education, HUD, SBA, and VA) and Treasury. It covers loan origination (both direct and guaranteed), loan servicing/lender monitoring, and debt collection.

This is a relatively new initiative of the President's Management Agenda. As such, the specific criteria to determine HUD's planned actions for the credit program initiative were only recently finalized. Achievement of the President's goal requires that the Agency focus on identifying and developing business requirements for changes to FHA single family loan products to meet the needs of the nation, and identify and modify the systems and processes to meet the new requirements. Additionally, FHA multifamily is developing a statement of governance for the

Business Process Reengineering effort related to multifamily accelerated processing and traditional application processing.

HUD has traditionally been a leader on OMB's Credit Program Policy Council, through efforts such as sharing and expanding FHA's Credit Alert Interactive Voice Response System (CAIVRS) process for use by all federal programs. Further, HUD has completed a number of significant internal control improvements to reduce the risk of the FHA Single Family Housing Mortgage Insurance Programs -- such as the implementation of the Credit Watch Termination Initiative and Appraiser Watch; updates to the Neighborhood Watch Early Warning System (lender and loan level risk management tool); and the implementation of the TOTAL automated underwriting process.

During FY 2008, as the nation experienced increasing numbers of mortgage foreclosures and the failure of large financial institutions, much of the Department's effort was focused on finding creative ways to address the nation's housing crisis, while maintaining FHA's strong underwriting criteria. Noting that the mortgage market had been drifting away from FHA insured loans and the mandatory underwriting standards that accompany them, in February of 2006, as part of the President's FY 2007 budget submission, FHA submitted a modernization proposal to provide greater flexibility for FHA-funded mortgages. The request sought legislative reform to increase FHA loan limits, create a risk-based premium structure, enhance flexibility for downpayment requirements, simplify requirements for condominium loans, expand the use of reverse mortgages, and increase access to pre- and post-purchase counseling for low- and moderate-income homeowners. Most of these modifications were included in the Housing and Economic Recovery Act of 2008 that was signed into law on July 30, 2008.

Also in FY 2007, FHA announced the *FHASecure* Program as a temporary measure to provide refinancing opportunities to homeowners with various types of ARMs. *FHASecure* gives qualified homeowners with non-FHA Adjustable Rate Mortgages the ability to refinance into a FHA-insured mortgage.

The sharp increase in mortgage foreclosures experienced during FY 2008 has occurred due to rising energy costs, increased joblessness, lax conventional underwriting, falling home prices, and resetting interest rates for adjustable rate subprime mortgages.

As HUD begins to implement the provisions of the new housing bill, the credit program management strategy will be refined, and the Department will continue its efforts to progress in this vital initiative.

ANALYSIS OF FINANCIAL CONDITION AND RESULTS

This section provides a summary of HUD's:

- Financial Data
- Analysis of Financial Position
- Analysis of Off-Balance Sheet Risk

Summarized Financial Data

(Dollars in Millions)

	2008	2007
Total Assets	$125,036	$111,074
Total Liabilities	$30,521	$20,360
Net Position	$94,515	$90,714
FHA Insurance-In-Force	$573,196	$399,960
Ginnie Mae Mortgage-Backed Securities Guarantees	$576,800	$427,600
Other HUD Program Commitments	$57,027	$65,472

Analysis of Financial Position

Assets - Major Accounts

Total Assets for fiscal year 2008, as reported in the Consolidated Balance Sheets, are displayed in Chart 1. Total Assets of $125.0 billion are comprised primarily of Fund Balance with Treasury of $85.5 billion (68.4 percent) and Investments of $28.6 billion (22.9 percent).

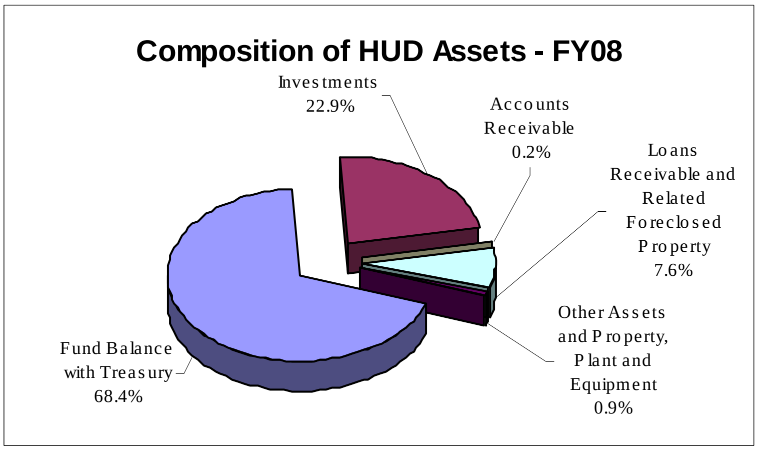


Chart 1 – Composition of HUD Assets –FY08

Total Assets increased $13.9 billion (12.5 percent) from $111.1 billion at September 30, 2007 to $125.0 billion at September 30, 2008. The net increase was due primarily to an increase of $16.5 billion (23.9 percent) in Fund Balance with Treasury from $69.0 billion at September 30, 2007 to $85.5 billion at September 30, 2008.

Table 1 presents total assets for fiscal year 2008 and the four preceding years. The changes and trends impacting Total Assets are discussed below.

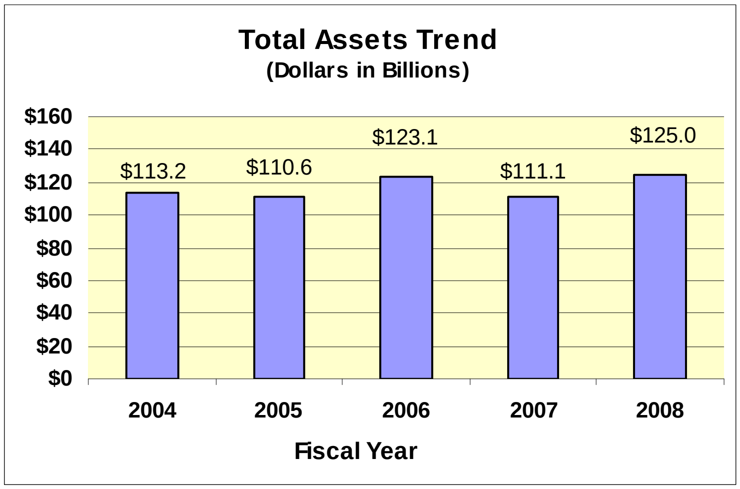


Table 1 – Total Assets Trend

Fund Balance with Treasury of $85.5 billion represents HUD's aggregate amount of funds available to make authorized expenditures and pay liabilities. Fund Balance with Treasury increased due to an increase of $8.2 billion in funding for the Community Development Block Program (CDBG), an increase in funding for Section 8 of $3.5 billion, and an increase in funding for FHA of $3.0 billion.

Investments of $28.6 billion consist primarily of investments by FHA's Mutual Mortgage Insurance/Cooperative Management Housing Insurance Fund and by Ginnie Mae, in non-marketable market-based Treasury interest-bearing obligations (i.e., investments not sold in public markets). Compared to last fiscal year, there was an insignificant net decrease in Investments.

Accounts Receivable of $0.24 billion primarily consists of claims to cash from the public and state and local authorities for bond refunding, Section 8 year-end settlements, sustained audit findings, FHA insurance premiums and foreclosed property proceeds. A 100 percent allowance for loss is established for all delinquent debt 90 days and over.

Loans Receivable and Related Foreclosed Property of $9.6 billion are generated by HUD's support of construction and rehabilitation of low rent housing, principally for the elderly and disabled under the Section 202/811 program, and FHA credit program receivables.

Remaining assets of $1.1 billion, comprising 0.9 percent of Total Assets, include fixed assets and other assets. Net changes pertaining to remaining asset balances increased by 33.9 percent compared to prior fiscal year.

Assets - Major Programs

Chart 2 presents Total Assets for fiscal year 2008 by major responsibility segment or program.

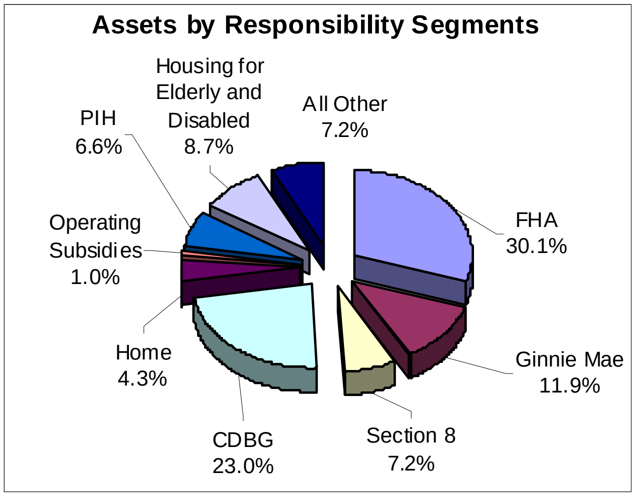


Chart 2 – Assets by Responsibility Segment

Liabilities – Major Accounts

Total Liabilities for fiscal year 2008, as reported in the Consolidated Balance Sheets, are displayed in Chart 3.

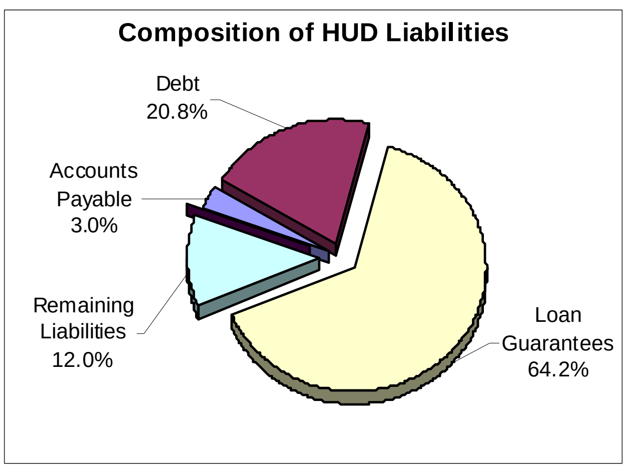


Chart 3 – Composition of HUD Liabilities

Total Liabilities of $30.5 billion consists primarily of debt in the amount of $6.3 billion (20.8 percent), loan guarantee liabilities of $19.6 billion (64.2 percent), accounts payable of $0.9 billion (3.0 percent), and remaining liabilities amounting to $3.7 billion (12.0 percent).

Total Liabilities increased $10.2 billion, 49.9 percent, from $20.4 billion at September 30, 2007 to $30.5 billion at September 30, 2008. The net increase in total liabilities was due primarily to an increase of $12.1 billion in Loan Guarantees offset by a net decrease of $1.9 billion in Remaining Liabilities.

Table 2 presents total liabilities for fiscal year 2008 and the four preceding years. A discussion of the changes and trends impacting Total Liabilities is presented in the subsequent paragraphs.

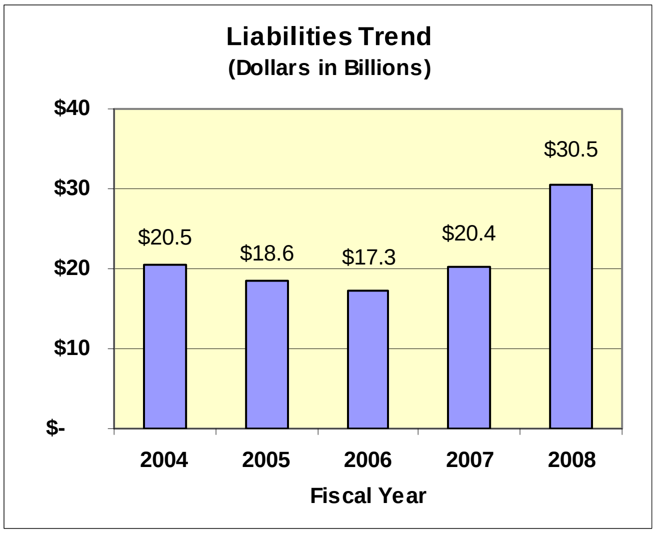


Table 2 – Liabilities Trend

Debt includes intra-governmental debt of $5.6 billion and debt held by the public of $0.7 billion. The intra-governmental debt consists of loans from the Treasury, Public Housing Authorities, Tribally Designated Housing Entities, Federal Financing Bank, and debentures issued by FHA in lieu of cash disbursements to pay claims. Debt held by the public consists of new housing authority bonds and FHA debentures issued to the public at par. The $0.1 billion decrease in debt (repayments exceed new borrowings) was due to a $0.2 billion increase in FHA debt and a decrease of $0.3 billion in PIH debt.

Accounts Payable consists primarily of pending grants payments and cash claims for single family properties and multifamily mortgage notes assigned.

Loan Guarantees consist of the liability for loan guarantees related to Credit Reform loans made after October 1, 1991 and the loan loss reserve related to guaranteed loans made before October 1, 1991. The liability for loan guarantees and the loan loss reserve are both comprised of the present value of anticipated cash outflows for defaults such as claim payments, premium refunds, property expense for on-hand properties, and sales expense for sold properties, less anticipated cash inflows such as premium receipts, proceeds from property sales, and principal interest on Secretary-held notes. The increase in loan guarantees of $12.1 billion was primarily due to an overall increase in guarantees for FHA programs.

Remaining liabilities of $3.7 billion consist primarily of Insurance Liabilities, Federal Employee and Veteran Benefits, and Other Liabilities. Net changes pertaining to remaining liability balances decreased by $1.9 billion, 12.0 percent, as compared to prior fiscal year.

Liabilities – Major Programs

Chart 4 presents Total Liabilities for FY 2008 by responsibility segment.

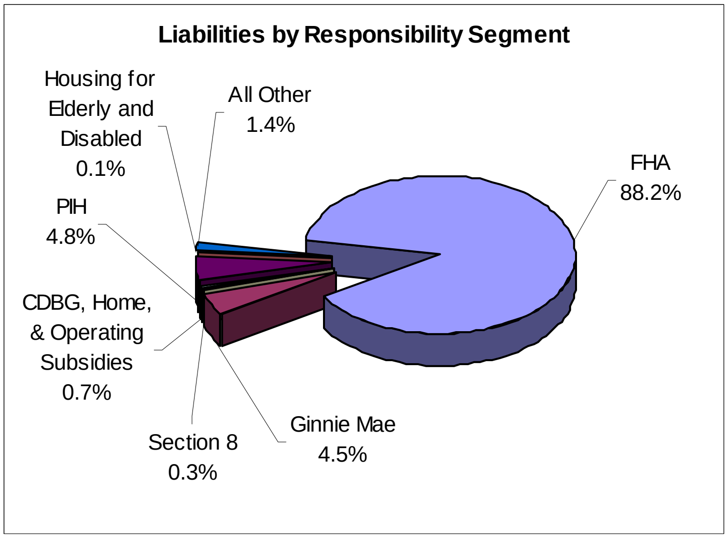


Chart 4 – Liabilities by Responsible Segment

Changes in Net Position

Changes in Unexpended Appropriations, Net Cost of Operations, and Financing Sources combine to determine the Net Position at the end of the year. The elements are further discussed below. Net Position as reported in the Statements of Changes in Net Position reflects an increase of $3.8 billion or 4.2 percent from the prior fiscal year. This increase in Net Position is primarily attributable to an $11.9 billion increase in Unexpended Appropriations and an $8.2 billion decrease in cumulative results of operations (Financing Sources in excess of Net Cost of Operations).

Unexpended Appropriations: which increased 21.9 percent from $54.5 billion in FY 2007 to $66.5 billion in FY 2008, represents the accumulation of appropriated funds not yet disbursed, and can change as the fund balance with treasury changes. A significant portion of these unexpended funds is attributable to long-term commitments as discussed in the following section.

Financing Sources: As shown in HUD's Statement of Changes in Net Position, HUD's financing sources (other than exchange revenues contributing to Net Cost) for FY 2008 totaled $49.0 billion. This amount is comprised primarily of $49.5 billion in Appropriations Used, offset by approximately $0.66 billion in net transfers out. The transfers out consist of new FHA subsidy endorsements, credit subsidy upward re-estimates and the sweep of the General Insurance/Special Risk Insurance liquidating account's unobligated budgetary resources.

Net Cost of Operations: as reported in the Consolidated Statements of Net Cost amounts to $57.2 billion for FY 2008, and reflects an 11.8 percent increase as compared to prior fiscal year. Net Cost of Operations consists of total costs, including direct and indirect program costs, as well as general Department costs, offset by program exchange revenues (received in exchange for services provided by HUD).

Table 3 presents HUD's Total Net Cost for FY 2008 by responsibility segment.

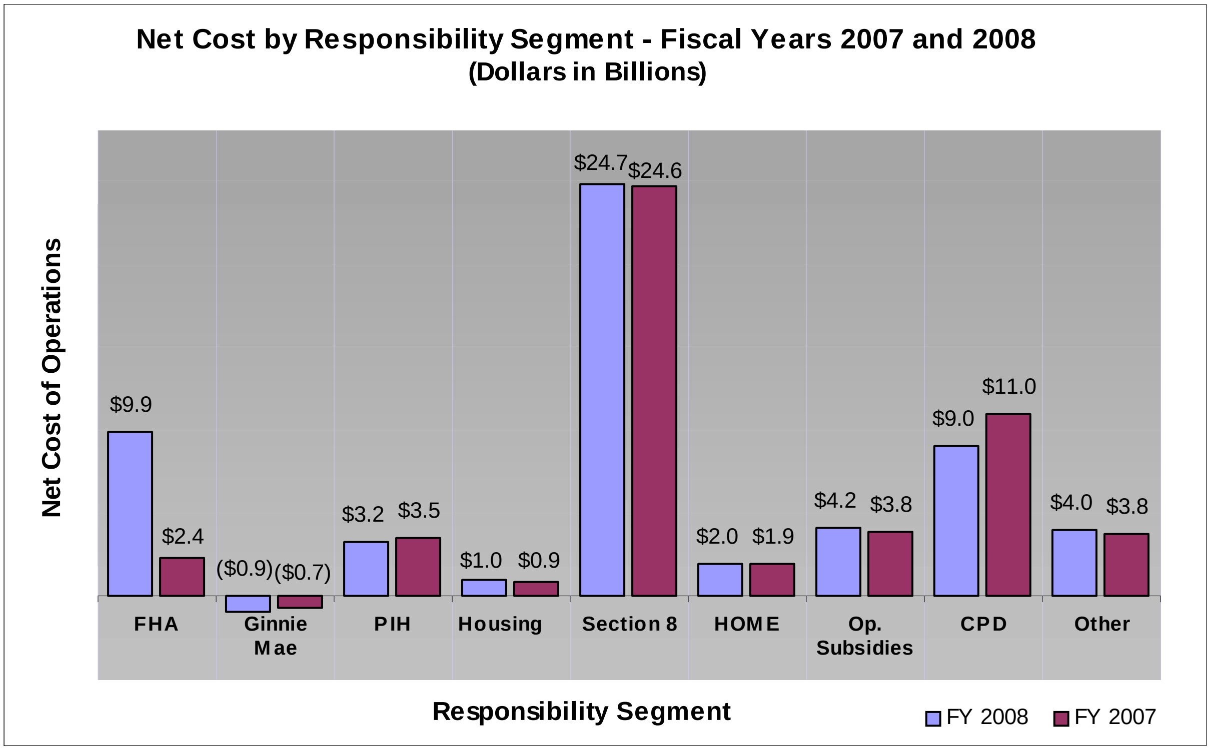


Table 3 – Net Cost by Responsibility Segment

As presented in Table 3, Cost of Operations was primarily a result of spending of $24.7 billion, 43 percent of Net Cost, in support of the Section 8 program (administered jointly by the Housing, Community Planning and Development, and PIH programs). The current fiscal year net cost of $24.7 billion for the Section 8 programs was $0.1 billion, or 0.4 percent, more than prior fiscal year. Total HUD Net Costs include FHA net loss of $9.9 billion attributable to FHA's upward re-estimate of the anticipated long-term costs of its insurance programs.

Net Results of Operations

The combined effect of HUD's Net Cost of Operations and Financing Sources resulted in a 155.3 percent change in Net Results of Operations of $8.2 billion during FY 2008. The significant year-to-year fluctuation shown in Table 3 is due primarily to the annual re-estimation of long-term credit program costs, which can be impacted by both program performance and economic forecasts.

Table 4 presents HUD's Net Results of Operations for FY 2008 and the four preceding years.

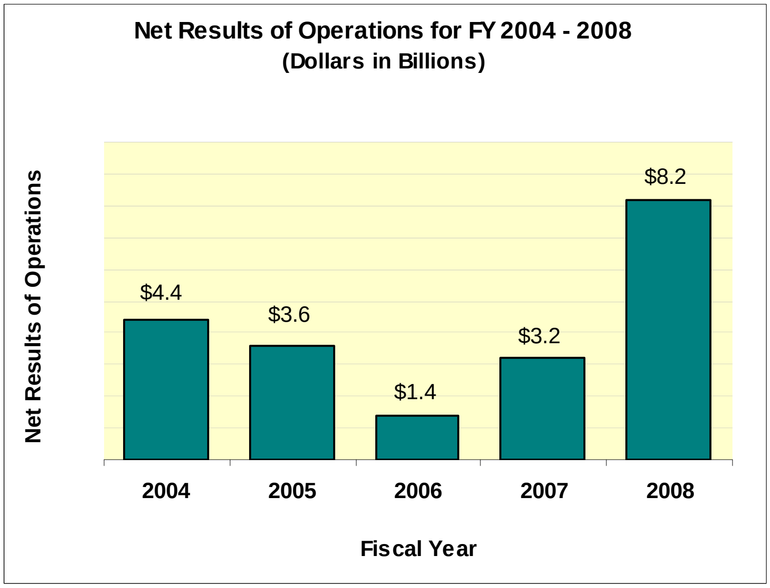


Table 4- Net Results of Operations Trend

Analysis of Off-Balance Sheet Risk

The financial risks of HUD's credit activities are due primarily to managing FHA's insurance of mortgage guarantees and Ginnie Mae's guarantees of mortgage-backed securities. Financial operations of these entities can be affected by large unanticipated losses from defaults by borrowers and issuers and by an inability to sell the underlying collateral for an amount sufficient to recover all costs incurred.

Contractual and Administrative Commitments

HUD's contractual commitments of $57.0 billion in FY 2008 represents HUD's commitment to provide funds in future periods under existing contracts for its grant, loan, and subsidy programs. Administrative Commitments (reservations) of $3.0 billion relate to specific projects for which funds will be provided upon execution of the related contract.

Table 5 presents HUD's Contractual Commitments for FY 2008 and the four preceding years.

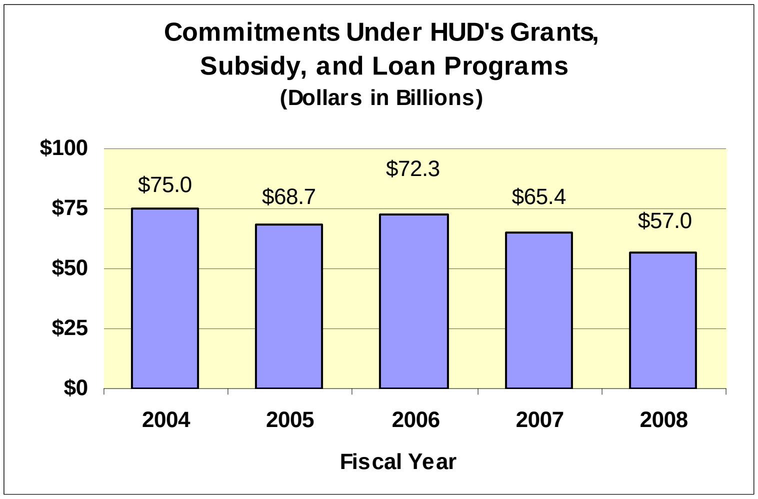


Table 5 – Commitments Under HUD's Grants, Subsidy and Loan Programs

These commitments are primarily funded by a combination of unexpended appropriations and permanent indefinite budget authority, depending on the inception date of the contract. HUD draws on permanent indefinite budget authority to fund the current year's portion of contracts entered into prior to FY 1988. Since FY 1988, HUD has been appropriated funds in advance for the entire contract term in the initial year, resulting in substantial increases and sustained balances in HUD's unexpended appropriations.

Total commitments (contractual and administrative) decreased $8.2 billion or 12.0 percent during FY 2008. The change is primarily attributable to a decrease of $2.5 billion in Section 8 commitments along with decreases of $3.0 billion in CDBG, $1.7 billion in Section 202/235/236, $0.4 billion in PIH, and $0.6 billion in All Other commitments.

Table 6 presents HUD's Section 8 Contractual Commitments for FY 2008 and the four preceding years.

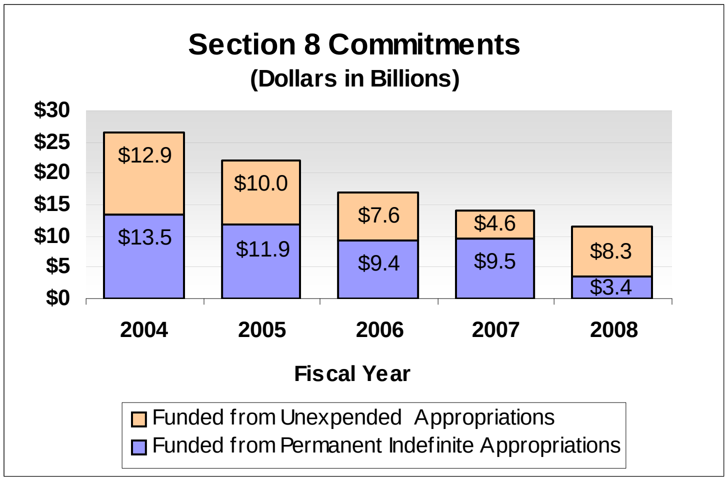


Table 6 – Section 8 Commitments

To contain the costs of future Section 8 contract renewals, HUD began converting all expiring contracts to 1-year terms during FY 1996. By changing to 1-year contract terms, HUD effectively reduced the annual budget authority needed from Congress to fund the subsidies while still maintaining the same number of contracts outstanding.

FHA Insurance in Force

FHA's total insurance-in-force increased $173.2 billion or 43.3 percent from $400.0 billion in FY 2007 to $573.2 billion in FY 2008. The increase in FHA's insurance-in-force was primarily due to higher endorsements in the last quarter of FY 2008 and an increase in the FHA reverse mortgage program (Home Equity Conversion Mortgages).

Table 7 presents FHA's Insurance in Force for FY 2008 and the four preceding years.

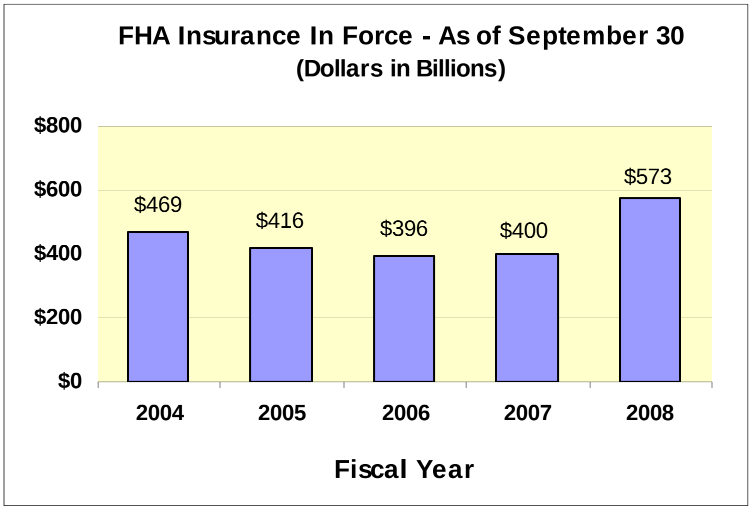


Table 7 – FHA's Insurance in Force at Year End

Ginnie Mae Guarantees

Ginnie Mae financial instruments with off-balance sheet risk include guarantees of Mortgage-Backed Securities and commitments to guaranty. 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, 2008 and 2007, was approximately $576.8 billion and $427.6 billion, respectively. Ginnie Mae's outstanding securities increased commensurate with endorsement volume increases at FHA. However, Ginnie Mae's potential loss is considerably less because the FHA and Rural Housing Service insurance and 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 Mortgage-Backed 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, 2008 and 2007 were $71.2 billion and $35.8 billion, respectively.

Table 8 presents Ginnie Mae Mortgage-Backed Securities for FY 2008 and the four preceding years.

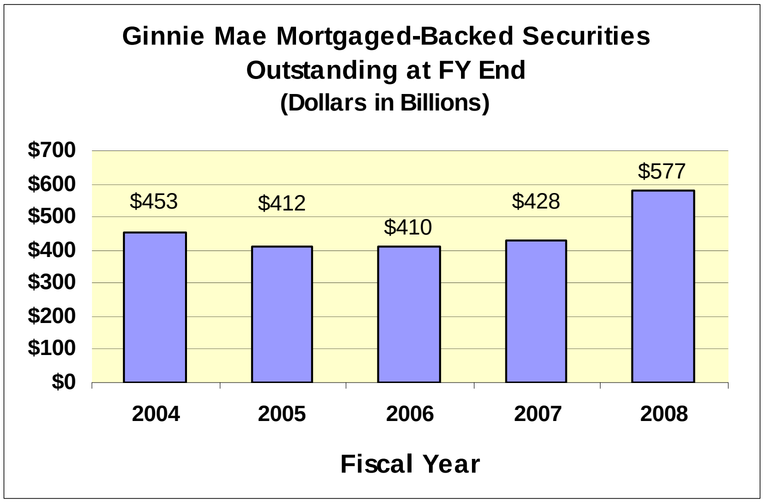


Table 8 – Ginnie Mae Mortgage-Backed Securities for FY 2008

Generally, Ginnie Mae's Mortgage-Backed 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 2008 and 2007, Ginnie Mae issued a total of $86.4 billion and $44.6 billion, respectively, in its multi-class securities program (REMICs, Stripped MBS, and Platinums). The estimated outstanding balance of multiclass securities in the total MBS securities balance at September 30, 2008 and 2007 were $253.1 billion and $201.0 billion, respectively. These securities do not subject Ginnie Mae to additional credit risk beyond that assumed under the Mortgage-Backed Securities program.

MANAGEMENT ASSURANCES

Federal Managers' Financial Integrity Act
Annual Assurance Statement for FY 2008

The Department of Housing and Urban Development's (HUD) management is responsible for establishing and maintaining effective internal controls and financial management systems that meet the objectives of the Federal Managers' Financial Integrity Act of 1982 (FMFIA), Sections 2 and 4. HUD conducted its assessment of the effectiveness of its internal control over the efficiency and effectiveness of opera`tions and compliance with applicable laws and regulations in accordance with OMB Circular A-123, *Management's Responsibility for Internal Control*. Based on the results of this evaluation, HUD can provide reasonable assurance that its internal control over the effectiveness and efficiency of operations and compliance with applicable laws and regulations as of September 30, 2008, was operating effectively and that no material weaknesses were found in the design or operations of the internal controls.

In addition, HUD conducted its assessment of the effectiveness of HUD's internal control over financial reporting, which includes safeguarding of assets and compliance with applicable laws and regulations in accordance with the requirements of Appendix A of OMB Circular A-123, *Management's Responsibility for Internal Control*. Based on the results of this evaluation, HUD can provide reasonable assurance that internal control over financial reporting, as of June 30, 2008, was operating effectively and no material weaknesses were found in the design or operation of the internal control over financial reporting.

The Federal Financial Management Improvement Act (FFMIA) requires federal agencies to implement and maintain financial management systems that are in substantial compliance with federal financial management systems requirements, federal accounting standards, and the United States Government Standard General Ledger at the transaction level. HUD provides reasonable assurance that its financial management systems substantially comply with FFMIA for FY 2008.

Steven C. Preston
Secretary
U.S. Department of Housing and Urban Development

Federal Managers' Financial Integrity Act

HUD management is responsible for establishing and maintaining effective internal controls and financial management systems that meet the objectives of the Federal Managers' Financial Integrity Act (FMFIA) and OMB Circular A-123, *Management's Responsibility for Internal*

Control. FMFIA requires agencies to establish internal controls over its operations. The controls include program, operational, and administrative areas, as well as accounting and financial management. It explains management's responsibility and role in the assessment of accounting and administrative internal controls. FMFIA Section 2 requires the agency head to annually assess and report on the effectiveness of its internal controls that protect the integrity of federal programs. FMFIA Section 4 requires the reporting of any material non-conformance with financial management systems prescribed in OMB Circular A-127, *Financial Management Systems* together with corresponding remediation plans. Additionally, FMFIA requires agencies to provide an annual statement of assurance regarding the effectiveness of internal and accounting controls over financial systems. OMB-Circular A-123 requires agencies to provide an assurance statement on management's assessment of the effectiveness of internal control over financial reporting as of June 30th of each fiscal year.

OMB Circular A-123 also requires agencies to identify the material weaknesses (MW) and significant deficiencies (SD) affecting the agency. The Government Accountability Office's July 2007 revision of *Government Auditing Standards* (also known as *The Yellow Book*) defines a control deficiency as follows: a deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, detect, or correct errors in assertions made by management on a timely basis. *The Yellow Book* defines a significant deficiency as a deficiency in internal control, or combination of deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected. According to *The Yellow Book*, a material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected.

HUD recognizes the importance of correcting material weaknesses and significant deficiencies in a timely manner. HUD continuously monitors the progress of corrective actions for all reported material weaknesses and significant deficiencies. This progress is discussed in the following sections.

Auditor Reported Material Weaknesses

HUD's Office of the Inspector General (OIG) reported two material weaknesses in the agency's FY 2007 Annual Consolidated Financial Statement Audit for the Federal Housing Administration's Home Equity Conversion Mortgage (HECM) program. HUD management disagreed with OIG that these issues warranted reporting as Material Weaknesses and reported them as a single Significant Deficiency. One material weakness is now closed and the other has been reduced to a significant deficiency as discussed in the next section.

Auditor Reported Material Weaknesses
FY 2007 Carry Over Issue and FY 2008 Status

First Reported	Auditor Reported Material Weakness	Status at End of FY 2008
2007	Develop a Risk Assessment and Systems Development Plan for FHA's HECM Systems and Transactions	Reduced to Significant Deficiency
2007	Enhance the HECM Credit Subsidy Cash Flow Model	Closed

The following tables provide a summary of financial audit findings in regards to audit opinion and management assurances. The first table is a summary of the results of the independent audit of HUD's consolidated financial statements, as well as information on the material weaknesses reported by HUD's auditors in connection with the FY 2007 Financial Statement Audit.

Summary of Financial Statement Audit

Audit Opinion	Unqualified				
Restatement	No				
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Ending Balance
FHA's Home Equity Conversion Mortgage Systems (HECM) Risk Assessment	1		1		0
HECM Credit Subsidy	1		1		0
Total Material Weaknesses	2		2		0

The second table is a summary of management assurances related to the effectiveness of internal control over HUD's financial reporting and operations, and its conformance with financial management system requirements under Sections 2 and 4, respectively, of the Federal Managers' Financial Integrity Act (FMFIA). The last portion of this table is a summary of HUD's compliance with the Federal Financial Management Improvement Act (FFMIA).

Summary of Management Assurances

Effectiveness of Internal Control over Financial Reporting (FMFIA § 2)						
Statement of Assurance	Unqualified					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
None	0	0	0	0	0	0
Total Material Weaknesses	0	0	0	0	0	0

Effectiveness of Internal Control over Operations (FMFIA § 2)						
Statement of Assurance	Unqualified					
Material Weaknesses	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
None	0	0	0	0	0	0
Total Material Weaknesses	0	0	0	0	0	0

Conformance with Financial Management System Requirements (FMFIA § 4)						
Statement of Assurance	Systems conform to financial management system requirements					
Non-Conformances	Beginning Balance	New	Resolved	Consolidated	Reassessed	Ending Balance
None	0	0	0	0	0	0
Total non-conformances	0	0	0	0	0	0

Compliance with Federal Financial Management Improvement Act (FFMIA)		
	Agency	Auditor
Overall Substantial Compliance	Yes	No
1. System Requirements	Yes	
2. Accounting Standards	Yes	
3. USSGL at Transaction Level	Yes	

Remaining Material Weakness Reclassified as Significant Deficiency

The Department's comprehensive strategy for addressing weaknesses in its internal controls over FHA's systems for processing HECM transactions and the lack of a documented program level risk assessment progressed to the point where the material weakness has been reclassified as a significant deficiency. In FY 2008, FHA's actions to mitigate this material weakness include performance of a comprehensive program risk assessment and completion of a privacy act assessment on the HECM Notes servicer. The HECM Notes servicer was evaluated via a Statement on Auditing Standards (SAS) Number 70, *Service Organizations,* Type I audit. FHA's FY 2009 plans to resolve this significant deficiency are as follows:

- To implement corrective actions resulting from the SAS 70 Type I audit in FY 2008;
- To conduct a SAS 70 Type II audit on the HECM Notes servicer that includes detailed testing over a six month period; and
- To procure a system development contractor to implement a new HECM information technology system in FHA.

Material Weakness – Closed

FHA's extensive FY 2008 efforts to resolve a material weakness that called for enhancements to the HECM Credit Subsidy Cash Flow Model were completed by the end of FY 2008. Actions taken to resolve this material weakness are described below.

- The HECM Cash Flow Model Documentation now addresses:
  - How specific assignment and termination rates are calculated and how macroeconomic projections are incorporated in the model;

  - Results of the current pricing and termination model reviews;
  - Previous HECM studies and how they informed the HECM Cash Flow Model;
  - How the HECM model replicates the methodology in OMB's Credit Subsidy Calculator 2 (CSC2) to calculate the HECM liability for loan guarantee (LLG);
  - How the HECM model discounts future cash flows in accordance with the OMB Circular A-11, *Preparation, Submission and Execution of the Budget*; and
  - How FHA has reviewed and improved its method for estimating note recoveries.
- All HECM Cash Flow Model changes and impacts were documented in accordance with the Configuration Management Plan.
- During the validation process, FHA now compares actual premium collections to model estimates. After validation and model changes, FHA internally reviews the HECM model and documents model changes in the configuration management memo prior to LLG estimation.
- The methodology of estimating the credit subsidy rate was reviewed and, per the request of OMB (as documented in the HECM Cash Flow Model Documentation Appendix), FHA did not incorporate the use of disbursements.
- FHA enhanced the functionality of the cash flow model to include a sensitivity analysis. Extraneous data was also removed from the cash flow model for ease of use.

Significant Deficiencies

HUD has demonstrated its commitment to resolving the significant deficiencies. The Department will report a significant deficiency as ***corrected*** when the following occurs:

- Corrective actions have been substantially completed;
- The remaining actions are minor in scope, and the actions will be completed within the next fiscal year; and
- Substantial validation of corrective action effectiveness has been performed.

Significant deficiencies continue to be reviewed internally by monitoring the progress of their corrective actions. HUD began FY 2008 with 12 significant deficiencies. Considerable progress was made to correct these significant deficiencies. At the end of FY 2008, HUD management determined that all but <u>one</u> should remain listed as Open deficiencies requiring further corrective action. FY 2008 accomplishments and remaining planned actions for each significant deficiency are provided in the following table.

STATUS OF REMAINING SIGNIFICANT DEFICIENCIES

SD 1 **Performance Measures**	**HUD needs to improve quality controls over performance measure data to ensure data: accuracy, timeliness, estimation, and availability.**
FY 2008 Accomplishments	• Completed two data quality assessments of performance measure data used to support Annual Performance Plan (APP) reporting. Supporting information systems were Interstate Land Sales/Real Estate Settlement Procedures Act system - RESPA module and Real Estate Management System.
Planned Actions	• Assess data quality of information systems whose data supports HUD's performance reporting.
Status at the end of FY 2008	**Open**
SD3 **PHA Monitoring**	**Continued efforts are needed to improve housing authority monitoring to ensure that program funds are expended in compliance with laws and regulations.**
FY 2008 Accomplishments	• Developed an internal tool to identify PHAs requiring on-site monitoring visits based on asset management. • Provided training to the Public Housing Revitalization Specialist (PHRS), Financial Analyst (FA), and Facilities Management (FM) staff members on conducting the monitoring reviews. • Conducted 101 Tier I monitoring activities for all PHAs selected during the risk assessment phase.
Planned Actions	• Modify the on-site monitoring strategy adding on-site monitoring reviews at the project level in addition to the comprehensive Tier 1 reviews. • Perform on-site management reviews on 180 selected Asset Management Projects.
Status at the end of FY 2008	**Open**

SD 4 **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.**
FY 2008 Accomplishments	• Obtained sufficient audit record storage capacity. • Established an audit reduction and report generation capability to support the fact investigations of security incidents. • Ensured that all Unisys security audit log events are monitored, analyzed, reported and followed up for the Unisys production system. • Restricted access to log files to those whose job function requires that access. • Improved monitoring and oversight for user access. • Developed procedures to routinely review accounts on General Support System (GSS) to disable/delete users with inactive accounts. • Continued process improvements to the Centralized HUD Account Management Process (CHAMP) and the migration of legacy data.
Planned Actions	• Investigate opportunities to begin system access removal procedures earlier in the employee separation to ensure terminated employees access is revoked in a timely manner. • Educate application owners on their responsibilities for removing user access and the associated process. • Ensure that any controls specific to the non-major application and required by NIST SP 800-53A are documented in the system security plans of the GSS. • Develop a plan to monitor the annual self assessments completed for GSS to ensure that all applicable security controls are reviewed and implemented by information technology contractors. • Establish security configuration baselines and perform periodic reviews of security configurations settings against the baseline to ensure the configurations match current security requirements. • Review database administrative practices to improve communication between database administrators and database owners.
Status at the end of FY 2008	**Open**

SD 7 **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.**
FY 2008 Accomplishments	• Implemented an automated payment process for the Section 235 Homeownership Program, utilizing the Department's Line of Credit Control System. • Implemented the Pay.gov process for the Excess Rental Income program in compliance with the Strategic Cash Management Agreement with Treasury. • Reviewed 95 percent of unliquidated obligations over the threshold ($217K for program funds and $17.5K for administrative funds). • De-obligated $9 million of program and administrative funds. • Recaptured $58 million of Section 236 Interest Reduction Program funds. • Developed additional management tools to better manage the de-obligation and recapture process. • Provided training to stakeholders and coordinated with the Office of the Chief Procurement Officer, the Office of the Chief Financial Officer, and the applicable program offices to determine contract validity and/or fund de-obligation or recapture eligibility. • Implemented a periodic review of terminated Rent Supplement and Rental Assistance Payments projects to ensure excess undisbursed contract authority is recaptured in a timely fashion.
Planned Actions	• Continue to perform quarterly reviews of unliquidated obligations. • Based on corrective actions completed in FY 2008, this issue is considered closed by management.
Status at the end of FY 2008	**Closed**
SD 13 **Resource Management**	**HUD needs to develop a comprehensive strategy to manage its resources and better estimate staffing needs and support its staffing requests.**
FY 2008 Accomplishments	• Continued reduction in competency gaps in leadership, mission critical occupations, human resources and information technology occupations. • Prepared of a gap analysis report and improvement plan by the Office of the Chief Procurement Officer for the acquisition occupation.

	• Implementation of "SMART" performance plans throughout HUD, including training on SMART for managers, supervisors, and employees. • Quarterly reporting to OPM on HUD's efforts in meeting OPM's 45-day hiring timeline for non-SES positions and the 61-day hiring timeline for SES positions. • Continued implementation HUD's Succession Management Plan, which included implementation of HUD Fellows Program and appointment of 2008 class of Emerging Leaders. • Prepared and submitted HUD's first Human Capital Accountability Report to OPM. • Initiated a Lean Six Sigma Business Process Re-engineering Study to accelerate and improve the staffing/ hiring process.
Planned Actions	• Continue efforts in closing skill gaps, which include establishing baseline gaps and targets for mission critical occupations throughout HUD. • Continue reporting to OPM on progress in meeting hiring timeline goals. • Continue implementing succession plan strategies. • Submit annually HUD's Human Capital Management Report to OPM. • Conduct an internal accountability review of the human resources program in one of the Field HR servicing offices. • Complete efforts to improve the end-to-end staffing/hiring process.
Status at the end of FY 2008	**Open**
SD 14 **Management Controls**	**Weaknesses in the Department's control environment impact HUD's ability to effectively manage its programs.**
FY 2008 Accomplishments	• Participated in HUD's Quality Management Reviews to assess Field Offices' operations. • Enhanced the reporting process for program offices to submit their annual FMFIA Internal Control Assurance Statement. • Issued A-123 Statement of Assurance on Internal Control over Financial Reporting.
Planned Actions	Conduct entity level internal control acquisition assessments as mandated by OMB Circular A-123.

	• Update guidance for a Front-End Risk Assessment of New or Substantially Revised Programs or Administrative Functions, in accordance with *Departmental Management Control Handbook, 1840.1 REV-3, Chapter 8*.
Status at the end of FY 2008	**Open**
<u>SD 16</u> 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.**
FY 2008 Accomplishments	• Developed a new Single Audit Act module in HUD's Audit Resolution and Corrective Action Tracking System and testing is underway. The new system will permit OIG personnel, HUD management officials, and Audit Liaison Officers to work in concert to track corrective actions and address identified deficiencies.
Planned Actions	• Implement the new system pending successful outcome of testing by the first quarter of FY 2009. • Complete the guide prior to implementation of the new system.
Status at the end of FY 2008	**Open**
<u>SD 18</u> Controls over Rental Housing Assistance	**Continued efforts are needed to improve housing authority monitoring to ensure that program funds are expended in compliance with laws and regulations.**
FY 2008 Accomplishments	• Conducted 101 "Tier 1" monitoring activities • Continued improvements in oversight and monitoring of subsidy calculations and intermediaries program performance by timely completing all monitoring activities. • Awarded a contract to perform: o Evaluation of the accuracy of how units were categorized. o Evaluation of the accuracy of HUD Form-52723, submitted to HUD. o Verification of the Utility Expense Level factor being used on the HUD Form-52723. o Research to determine the applicability and benefit of a checklist to be used by PHAs to identify the source documents.

	• Issued an Operating Subsidy Review Guide. • Completed a thorough review of all operating subsidy calculations by the Subsidy and Grants Information Systems (SAGIS) and on the excel tool submitted by housing authorities. • Conducted Training at the National Association of Housing and Redevelopment Officials meetings on the requirements of the new subsidy calculation and SAGIS requirements. • Provided Enterprise Income Verification (EIV) Training to all HUB and Program Centers. • Instituted the EIV to reduce the improper reporting of wages. • Conducted 92 Voucher Management System (VMS) onsite reviews. • Made funding available to cover the increased scope of A-133 audits. • Developed and trained staff to review Financial Assessment Sub-System (FASS) submissions. • Developed Utilization and Net Restricted Assets-Housing Assistance Payment (NRA-HAP) tools for the Field. • Converted Section 8 projects under the FMC payment process to Performance Based Contract Administrator contracts under Housing. • Converted the remaining portfolio of the traditional Contract Administrators' Section 8 contracts back into the Housing's accounting system.
Planned Actions	• Comprehensive reviews will continue and will be supplemented by 420 reviews at selected PHAs on asset management. • Update validation edits in VMS. • Develop a FASS/VMS NRA validation model. • Update PIC to collect additional subsidy and Low Income Tax Credit information. • Implement "mandatory EIV use" policy.
Status at the end of FY 2008	**Open**
SD 19 **Departmental Financial Management Systems**	**Lack of an integrated financial system in compliance with all federal financial management system requirements.**

FY 2008 Accomplishments	• Examined and documented 18 OCFO financial management systems and their interfaces with HUD Program Office systems and external business partner systems to document and verify 114 interfaces with supporting functional descriptions, data elements / data file layouts, technical requirements, and quality assurance actions in preparation for HUD Integrated Financial Management Improvement Project (HIFMIP) systems implementation / integration. • Automated the HECM Notes interface to the FHA Subsidiary Ledger.
Planned Actions	• Implement the core systems modernization HIFMIP strategy as discussed in the following systems section. • Support business process engineering and related development and configuration work to adapt the FHA Subsidiary Ledger to new processes for HECM financial operations. • Support business process engineering and related development and configuration work to adapt the FHA Subsidiary Ledger to new FHA Modernization, Hope for Homeowners, and Manufactured Housing insurance programs mandated by the Housing and Economic Recovery Act.
Status at the end of FY 2008	**Open**
SD 20 **Section 8 Project-Based Housing Assistance Payment Contracts**	**Improved controls are needed for budgeting, renewing, amending and paying Section 8 Project-Based Housing Assistance Payment Contracts**
FY 2008 Accomplishments	• Performed a detailed review to ensure that PAS data on Section 8 project-based contracts used to compute obligation balances is accurate and reliable.
Planned Actions	• Develop a long-term financial management system solution to streamline and automate the overall Section 8 project-based budgeting, payment, and contract management process. • Consider revising current Section 8 Project-base recapture methodology to include recapturing funds from expired Section 8 contracts. • Complete development of a Section 8 Project Based Assistance reporting structure using the Financial Data Mart.

Status at the end of FY 2008	**Open**
<u>SD 21</u> HECM Credit Subsidy Cash Flow Model	**Improved quality controls are needed to ensure accurate data is entered into the Home Equity Conversion Mortgage (HECM) Model.**
FY 2008 Accomplishments	• Enhanced documentation on how specific assignment and termination rates are calculated and how macroeconomic projections are incorporated. • Developed the HECM cash flow model to reflect current and future cash flows of the HECM program. • Performed a comprehensive program risk assessment. • Developed the requirements for a new HECM system and procurement for a contractor is in progress. • Completed a privacy act assessment on the HECM Notes servicer. • Performed a SAS 70 Type I review on the HECM Notes servicer. • Directed application system owners to fully assume the roles and responsibilities of system owners in accordance with *HUD Handbook 2400.25 REV-1, Information Technology Security Policy*. • Mandated a role-based training program for FHA program staff with significant information security responsibilities.
Planned Actions	• Complete SAS 70 Type II audit and implement remaining corrective actions identified in the Type I audit. • Procure a system development contractor to implement a new HECM information technology system.
Status at the end of FY 2008	**Open**
<u>SD 22</u> Ginnie Mae Mortgage-Backed Securities (MBS) Monitoring	**Improved program compliance and controls regarding monitoring of issuers are needed.**

FY 2008 Accomplishments	• Instituted a new reporting process where Ginnie Mae senior management will be provided information to improve communication of issuers that are not in compliance with program requirements. • Reviewed and strengthened the completeness and timeliness of the automated pool collateral matching process as well as follow-up on unmatched loans with issuers. Full implementation of this process is scheduled for FY09.
Planned Actions	• Segregation of duty issues enumerated by OIG will be alleviated when Ginnie Mae fills the position of Senior Vice President of the Office of Mortgage-Backed Securities which is scheduled for early FY09. • Refine and complete implementation of the automated pool collateral matching process.
Status at the end of FY 2008	**Open**

SYSTEM NON-CONFORMANCE ISSUES

Section 4 of FMFIA provides the requirements for reporting instances of material non-conformance with the criterion, which includes preparing remediation plans that address each non-conformance. OMB Circular A-127 and the Federal Financial Management Improvement Act of 1996 (FFMIA) established federal financial management system criteria. Financial management systems are compliant when they fulfill the 12 requirements outlined in OMB Circular A-127, Section 7. OMB guidelines specify that departments and agencies are substantially compliant with FFMIA when 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.

A system is considered non-conforming when it does not comply with the required factors. The materiality or severity of the impact of non-conformance is evaluated against the overall capability of the system to consistently generate accurate, reliable, financial information required for effective and efficient agency management.

During FY 2008, HUD's financial systems substantially complied with FFMIA. We maintained our focus on successfully implementing an aggressive approach toward resolving past financial system non-conformance concerns. The next section details HUD's strategy for meeting this requirement.

STATUS OF REMAINING SYSTEMS NON-CONFORMANCE ISSUES

HUD is currently engaged in the development of a major financial systems modernization project. The HUD Integrated Financial Management Improvement Project (HIFMIP) establishes an enterprise vision to achieve a core financial management system as a resolution to the Department's integration and modernization efforts. In FY 2008, HUD committed its efforts to a continued enhanced development of its departmental financial management systems as discussed below.

(a) The Federal Housing Administration (FHA) continued to improve its financial management through the phased implementation of an integrated financial management system to better support FHA's business needs, respond to internal and external conformance requirements, and adequately safeguard agency resources from mismanagement, fraud, waste, and abuse.

(b) An Integrated Procurement Team (IPT) continued to conduct a full and open competition to select a qualified service provider to support the integration of the Department's legacy core accounting system to the new Commercial Off-The-Shelf (COTS) federally certified software system. Concurrently, three major program organizations within the Department are completing their own financial systems modernization projects and are scheduled to integrate those system functions to the enterprise core financial management system.

(c) The Office of the Chief Financial Officer (OCFO) developed an incremental project approach to ensure that integration of the three systems would be accomplished with minimal disruption to ongoing operations, given the complexity and large number of programs managed by the Department. The project timeline and established goal to achieve full integration is FY 2013.

(d) The OCFO developed a roadmap to support a phased integration of the three core financial systems currently maintained by the Department. After retirement of two systems, 14 of the 16 legacy systems remain of those systems originally identified for consolidation or retirement.

A complete listing of Departmental financial and mixed financial management systems is shown in Section 4. All agency financial systems undergo an annual self-assessment by the system owner, and are subject to an independent validation review to ensure they remain compliant. At the end of FY 2008, two financial systems, the HUD Procurement System (HPS) and the Small Purchase System (SPS), remained non-compliant.

Remediation plans for HPS and SPS were developed by the Office of the Chief Procurement Officer (OCPO). The plans fully addressed the financial management system compliance and regulatory requirements. Since the development of the remediation plans, it was determined that it would be more cost effective to acquire a new system than to modify the existing systems. The replacement system is referred to as "HUD Integrated Acquisition Management System" (HIAMS). Due to limited funding to develop HIAMS, OCPO has implemented compensating controls to mitigate their noncompliance issues. Based on the implementation of compensating controls, HUD believes these systems do not warrant being reported as non-conforming under Section 4 of FMFIA.

FEDERAL INFORMATION SECURITY MANAGEMENT ACT

The Federal Information Security Management Act of 2002 (FISMA) requires each agency to generate "…a comprehensive framework for ensuring the effectiveness of information security controls over information resources that support Federal operations and assets…" It assigns specific responsibilities to Federal agencies, the National Institute of Standards and Technology (NIST), and the Office of Management and Budget (OMB) in order to strengthen information system security. In particular, FISMA requires an agency's head to implement policies and procedures to cost-effectively reduce information technology security risks to an acceptable level and to annually report to OMB on the effectiveness of the agencies' security programs.

HUD relies extensively on Information Technology to carry out its operations. The agency continues to improve its Information System Security Program. The implemented improvements during FY 2008 increase HUD's ability to protect the availability, integrity, and confidentiality of information stored on its systems. HUD's noted accomplishments include certification and accreditation of 100 percent of HUD's general support systems and major applications, conducting privacy impact assessments, issuing a NIST compliant IT Security Policy, and providing a more comprehensive Security Awareness training.