



OFFICE of
INSPECTOR GENERAL
★ ★ ★ ★
UNITED STATES DEPARTMENT OF
HOUSING AND URBAN DEVELOPMENT

The City and County of Honolulu Should Enhance Its Fraud Risk Management Practices for Its ESG CARES Act Program

Audit Report Number: 2024-LA-1002

August 6, 2024

To: Mark Chandler
Director, Office of Community Planning and Development, Honolulu Field Office, 9CD

//signed//

From: Kilah S. White
Assistant Inspector General for Audit, Office of Inspector General, GA

Subject: The City and County of Honolulu, HI, Should Enhance Its Fraud Risk Management Practices for Its ESG CARES Act Program

Attached are the U.S. Department of Housing and Urban Development (HUD), Office of Inspector General's (OIG) final results of our review of the City and County of Honolulu's fraud risk management for its Emergency Solutions Grants Coronavirus Aid, Relief, and Economic Security Act program.

HUD Handbook 2000.06, REV-4, sets specific timeframes for management decisions on recommended corrective actions. For each recommendation without a management decision, please respond and provide status reports in accordance with the HUD Handbook. Please furnish us copies of any correspondence or directives issued because of the audit.

The Inspector General Act, as amended, requires that OIG post its reports on the OIG website. Accordingly, this report will be posted at <https://www.hudoig.gov>.

If you have any questions or comments about this report, please do not hesitate to call Tanya Schulze, Audit Director, at (213) 534-2471.

Highlights

The City and County of Honolulu Should Enhance Its Fraud Risk Management Practices for Its ESG CARES Act Program | 2024-LA-1002

What We Audited and Why

We audited the City and County of Honolulu’s Department of Budget and Fiscal Services’ and Department of Community Services’ (City) fraud risk management practices for its Emergency Solutions Grants Coronavirus Aid, Relief, and Economic Security Act (ESG CARES Act) program with the objective of assessing the maturity of the City’s fraud risk management framework that encompasses control activities to prevent, detect, and respond to fraud. Fraudulent activity in the ESG CARES Act program can lead to significant financial losses; reputational damage to the grantee and the U.S. Department of Housing and Urban Development (HUD); breach of fiduciary duty; and, most importantly, loss of funding for individuals and families who are homeless or receiving homeless assistance or other homelessness prevention activities. Robust antifraud activities will help ensure that pandemic grant funds are put toward their intended uses and that funds are spent effectively and assets are safeguarded. HUD relies on its grantees to detect and prevent fraud, waste, and abuse.

Congress provided \$4 billion for the ESG CARES Act program, which represented a 1,379 percent increase to the regular 2020 annual ESG appropriation. Given the influx of fundings, we initiated a series of audits examining ESG CARES Act grantees’ fraud risk management practices and evaluating whether selected ESG CARES Act grantees are adequately prepared to prevent, detect, and respond to fraud. We selected the City to audit because it was authorized more than \$25 million in ESG CARES Act program funds, a 3,640 percent funding increase from its formula ESG allocation for fiscal year 2020. Large influxes of funding on an emergency basis can pose additional challenges for grantees that must also ensure adequate controls over the funding.

What We Found

The City did not adequately develop a fraud risk management framework for the ESG CARES Act program to prevent, detect, and respond to fraud. The City’s approach to fraud risk management was reactive, not proactive, and it did not institute robust antifraud practices resulting in the lowest maturity level (ad hoc¹) for organizations’ antifraud initiatives. The City had implemented some specific fraud controls and activities but did not implement best practices, including (1) establish a dedicated antifraud component to design and oversee fraud risk management activities, (2) promote fraud awareness throughout its departments, (3) perform a fraud risk assessment or develop a process to regularly conduct such assessments, (4) consider the use of data analytic tools to identify potential fraud, (5) have a dedicated hotline for external entities to report fraud for the ESG CARES Act program, or (6) have a process to evaluate the effectiveness of fraud risk management activities. This condition occurred because the City was

¹ The U.S. Chief Financial Officers Council and the U.S. Department of Treasury, Bureau of the Fiscal Service developed Program Integrity: The Antifraud Playbook that contains a maturity model designed to help agencies assess and identify the current state and goal state of their antifraud program and related efforts. The maturity model includes four progressive levels of fraud maturity. The lowest maturity level is ad hoc.

not aware of significant fraudulent activity for the program and HUD did not require a fraud risk management framework. As a result, the \$25.6 million allocated to the City for the ESG CARES Act program is at an increased risk of fraud.

What We Recommend

We recommend that the Director of HUD's Honolulu Office of Community Planning and Development instruct the City to (1) improve or enhance its antifraud efforts for the ESG program and incorporate fraud risk management practices that are consistent with fraud risk management best practices and (2) obtain training or technical assistance as needed on the implementation of fraud risk management best practices.

Table of Contents

| | |
|--|-----------|
| Background and Objective | 1 |
| Results of Audit | 5 |
| The City and County of Honolulu Should Enhance Its Fraud Risk Management Practices for Its ESG CARES Act Program | 5 |
| Scope and Methodology | 11 |
| Appendixes | 12 |
| Appendix A – Auditee and HUD Comments and OIG’s Evaluation | 12 |

Background and Objective

On March 11, 2020, the World Health Organization characterized the outbreak of the coronavirus disease 2019 (COVID-19) as a pandemic. In response, Congress provided \$4 billion in the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) for the Emergency Solutions Grants (ESG) program to use to “prevent, prepare for, and respond to coronavirus, among individuals and families who are homeless or receiving homeless assistance and to support additional homeless assistance and homelessness prevention activities to mitigate the impacts created by coronavirus.” This additional funding could be used to provide (1) emergency shelter, (2) temporary emergency shelter, (3) rapid rehousing, (4) homelessness prevention assistance, and (5) other crisis response activities. The funding was provided in two rounds of funding, as follows:

- Round 1: \$1 billion allocated under the ESG formula to grant recipients.
- Round 2: \$2.96 billion allocated under a formula targeted toward communities with a high incidence of sheltered and unsheltered homeless and those at the greatest risk for homelessness.

HUD moved quickly to make COVID-19 relief funding available to communities across the Nation. Between 2020 and 2022, HUD awarded the City and County of Honolulu (City) \$25.6 million in ESG CARES Act funds in three separate allocations, as shown in table 1. This amount represents a 3,640 percent funding increase from its annual formula ESG grant allocation for 2020. The City allocated most of its funding for emergency shelters and rapid rehousing (\$22.2 million in total, or 87 percent).²

Table 1: Funding allocated to the City between 2020 and 2022 (as of May 30, 2024)

| Allocation | Contract date | Allocation amount | Total disbursed | Balance | ESG CARES Act expenditure deadline |
|----------------------------|--------------------|---------------------|---------------------|------------------|------------------------------------|
| ESG CARES Act 1 | July 07, 2020 | \$2,429,569 | \$2,429,569 | - | September 30, 2023 |
| ESG CARES Act 2 | February 19, 2021 | 22,370,813 | 22,370,813 | - | September 30, 2023 ³ |
| ESG CARES Act Reallocation | September 22, 2022 | 849,017 | 1,872 | 847,145 | June 30, 2024 |
| Total ESG CARES Act | | \$25,649,399 | \$24,802,254 | \$847,145 | |

² Of that total, \$11.9 million was awarded to subrecipients for emergency shelters, and \$10.3 million was awarded to subrecipients for rapid rehousing.

³ HUD’s Office of Community Planning and Development Notice 22-06 states that recipients must spend all amounts awarded through the first and second allocations of ESG CARES Act funds by September 30, 2023, except for administration and Homeless Management Information System funds necessary for ESG CARES Act closeout, which must be spent by December 31, 2023. Also, 2 CFR (Code of Federal Regulations) 200.344 states that unless the Federal awarding agency or pass-through entity authorizes an extension, a non-Federal entity must liquidate all financial obligations incurred under the Federal award no later than 120 calendar days after the end date of the period of performance as specified in the terms and conditions of the Federal award.

City and County of Honolulu

There are two departments within the City that are involved with the administration of the ESG CARES Act program. The Community Based Development Division within the Department of Community Services administers programs and implements projects designed to preserve and expand the supply of affordable housing for low- and moderate-income households, address the shelter and service needs of City residents who are experiencing homelessness or have special needs, support community development initiatives, and affirmatively furthers fair housing. This division is primarily responsible for the management and oversight of the ESG CARES Act program. The Department of Budget and Fiscal Services is the City's central financial agency and is responsible for the accounting transactions and conducting monitoring reviews for the ESG CARES Act program.

Fraud Risk Management

Fraud risk management helps to ensure program integrity by continuously and strategically mitigating both the likelihood and effects of fraud. When fraud risks can be identified and mitigated, fraud may be less likely to occur. Although the occurrence of fraud indicates that there is a fraud risk, a fraud risk can exist even if actual fraud has not yet occurred or been identified. Effectively managing fraud risk helps to ensure that programs fulfill their intended purpose, funds are spent effectively, and assets are safeguarded. A fraud risk management framework can assist organizations in accomplishing these goals.

The COVID-19 pandemic significantly changed the operating landscape of Federal, State, and local governments. The substantial increase in funding associated with the pandemic relief funds also increased opportunities for fraud. For the ESG program, Congress provided an additional \$4 billion through the CARES Act, placing increased importance on grantees to proactively react in kind through improving or revamping their processes and overall governance structure to keep pace. Building, designing, and implementing a robust fraud risk management framework will aid in mitigating risks and decreasing the likelihood of fraud. Effectively managing fraud risk helps to ensure that grant funds are put toward their intended uses, funds are spent effectively, and assets are safeguarded.

Grantees should not only consider fraud risk management practices for pandemic funding, but also consider these best practices portfolio wide since grantees receive Federal funds from HUD as well as other Federal agencies. For example, a grantee's fraud risks, and controls to mitigate them, might be applicable to multiple Federal grant programs.

According to the U.S. Government Accountability Office's (GAO) Standards for Internal Control in the Federal Government⁴ and the Committee of Sponsoring Organizations' (COSO) Internal Control

⁴ On September 10, 2014, GAO updated the Standards for Internal Control in the Federal Government, which sets the standards for an effective internal control system for Federal agencies and provides the overall framework for designing, implementing, and operating an effective internal control system. Originally issued in November 1999, the Standards for Internal Control in the Federal Government is known as the Green Book. The Green Book may be adopted by State, local, and quasi-governmental entities as a framework for an internal control system.

Integrated Framework,⁵ assessing the risk of fraud is one of many principles for establishing an effective internal control system. In addition, due to the importance of this principle, both organizations have published fraud risk management guides with the intention to support organizations in meeting this principle. GAO and COSO make it clear that for a system of internal control to be effective, each of the principles, including “assessing the risk of fraud,” must be present, functioning, and operating together in an integrated manner. The regulations at 2 CFR (Code of Federal Regulations) 200.303 state that non-Federal entities must establish and maintain effective internal control over Federal awards and are recommended to follow GAO’s Standards for Internal Controls in the Federal Government or COSO’s Internal Control Integrated Framework.

GAO has noted that “[f]raud poses a significant risk to the integrity of federal programs and erodes public trust in government.” GAO’s Standards for Internal Control in the Federal Government defines fraud as obtaining something of value through willful misrepresentation and states that management should consider the potential for fraud when identifying, analyzing, and responding to risks. In July 2015, GAO issued A Framework for Managing Fraud Risks in Federal Programs.⁶ The primary audience of the Framework is managers in the U.S. Federal Government, but the leading practices and concepts described in the Framework may also be applicable to State, local, and foreign government agencies, as well as nonprofit entities that are responsible for fraud risk management. The Framework identified leading practices; encompassed control activities to prevent, detect, and respond to fraud; and identified four components – (1) assess, (2) design and implement, (3) evaluate and adapt, and (4) commit – for effectively managing fraud risks.

The U.S. Chief Financial Officers Council (CFOC) and the U.S. Department of the Treasury, Bureau of the Fiscal Service (BFS), developed Program Integrity: The Antifraud Playbook in October 2018 for use by the entire financial management community, including Federal, State, and local agencies. The Antifraud Playbook contains a maturity model designed to help agencies assess and identify the current state and goal state of their antifraud program and related efforts. The maturity model includes four progressive levels of fraud risk maturity, which are defined below from the lowest to highest desired goal state.

Ad hoc – Fraud risk management processes are disorganized, even chaotic, and antifraud efforts are undocumented and in a state of dynamic change, tending to be driven in an ad hoc, uncontrolled, and reactive manner. This is not a goal state for agencies with fraud exposure.

Initial – The agency is aware of the need for a more formal fraud risk management approach, and repeatable processes have been developed. Risks are still managed largely in a reactive way.

Operational – Fraud risk management activities across the organization are aligned with controls, and information on fraud risks is aggregated and analyzed and is easily available to the necessary individuals. The goal state for agencies with low fraud risk exposure is an initial to operational maturity level.

Leadership – The agency’s focus is on continually improving fraud risk management through both incremental and innovative changes or improvements. Risks are managed largely in a proactive

⁵ In May 2013, COSO published the Internal Control – Integrated Framework to enable organizations to effectively and efficiently develop and maintain systems of internal control.

⁶ GAO-15-593SP, issued July 28, 2015.

way. The goal state for agencies with high fraud exposure is an operational to leadership maturity level.

Further, the Antifraud Playbook organizes fraud risk management into the following four phases: (1) create a culture, (2) identify and assess, (3) prevent and detect, and (4) insight into action.

HUD Fraud Risk Management

HUD is responsible for designing its programs such that there are sufficient controls to support robust fraud risk management practices. The Payment Integrity Information Act of 2019, and implementing guidance from OMB, require HUD to establish financial and administrative controls to identify and assess fraud risks. OMB circular A-123 specifically requires that Departments like HUD incorporate leading practices from GAO's Green Book as well as the Fraud Risk Framework. In turn, HUD policy implementing OMB A-123 guidance says that HUD managers must design, implement, and operate processes with controls that mitigate the risk of fraud, waste, and abuse in HUD programs. It also says that to determine the effectiveness of fraud risk management activities, HUD program and support managers will "routinely evaluate existing fraud risk controls".

HUD OIG's October 2021 audit, "Fraud Risk Inventory for the CDBG and ESG CARES Act Funds", noted several opportunities for HUD to improve its fraud risk management practices in its ESG CARES Act program. The audit noted that CPD did have existing controls that could detect fraud, such as monitoring reviews, but that they could be improved through the implementation of a fraud risk checklist or other instrument during CPD's monitoring activities. The audit also inventoried specific ways in which the ESG CARES Act program could be defrauded. Importantly, during that audit, HUD noted that it expects its grantees to be proactive in the identification and remediation of fraud, and that the responsibility for the assessment and mitigation of fraud risks rests primarily with the grantees.

Our audit objective was to assess the City's fraud risk management framework for its ESG CARES Act program, which encompasses control activities to prevent, detect, and respond to fraud.

Results of Audit

The City and County of Honolulu Should Enhance Its Fraud Risk Management Practices for Its ESG CARES Act Program

The City did not adequately develop a fraud risk management framework for its ESG CARES Act program to prevent, detect, and respond to fraud, resulting in the lowest maturity level (ad hoc) for organizations' antifraud initiatives. The City's approach to fraud risk management was reactive, not proactive, and it did not institute robust antifraud practices because it was not aware of recent significant fraudulent activity for the program. However, without a fraud risk management framework in place, there was an increased risk of undetected and unreported fraud. The City had implemented some specific fraud controls and activities such as a reviewing supporting documentation for all payment requests, but did not include best practices, such as (1) establishing a dedicated antifraud component to design and oversee fraud risk management activities, (2) promoting fraud awareness throughout its departments, (3) performing a fraud risk assessment or develop a process to regularly conduct such assessments, (4) considering the use of data analytic tools to identify potential fraud, (5) having a dedicated hotline for external entities to report fraud for the ESG CARES Act program, and (6) having a process to evaluate the effectiveness of fraud risk management activities. Also, although CPD previously stated that the responsibility for the assessment and mitigation of fraud risks rests primarily with the grantees, HUD did not require its ESG CARES Act grantee to develop systematic antifraud activities or provide technical assistance in doing so. As a result, the \$25.6 million allocated to the City for the ESG CARES Act program is at an increased risk of fraud.

The City's Fraud Risk Management Practices Should Be Improved

We assessed the current state of the City's fraud risk management practices for the ESG CARES Act program using the Antifraud Playbook's Program Maturity Model, which organizes the four phases of fraud risk management into the following: (1) create a culture, (2) identify and assess, (3) prevent and detect, and (4) insight into action.⁷ Our review concluded that the City's overall fraud risk management practices were at the lowest maturity level and that there were opportunities to improve its antifraud efforts to better identify and protect against fraud. To achieve the highest maturity level, the City would need to follow the best practices in antifraud programs, as published by organizations such as GAO⁸ and COSO.⁹

Phase 1 – create a culture maturity level: The City did not assess fraud or promote fraud awareness.

The Antifraud Playbook encourages organizations to build a culture that is conducive to both integrity efforts and furthering antifraud measures at the organization, including through understanding how

⁷ CFOC's and Treasury BFS's Antifraud Playbook identifies 16 leading practices for effective fraud risk management organized into 4 phases of action. The results of our audit are aligned to match the Antifraud Playbook's four-phased approach.

⁸ To help managers combat fraud and preserve integrity in government agencies and programs, GAO identified leading practices for managing fraud risks and organized them into a conceptual framework called the Fraud Risk Management Framework.

⁹ COSO partnered with the Association of Certified Fraud Examiners in 2016 to create the Fraud Risk Management Guide. The joint report is designed to aid organizations in effectively establishing an overall fraud risk management program.

vulnerable an organization is to fraud (that is, “fraud exposure”). GAO’s Framework for Managing Fraud Risks in Federal Programs provides that management should create an organizational culture to combat fraud at all levels of the organization and have a dedicated entity to lead the fraud risk management activities. Our assessment of the City’s maturity within this phase identified its status as “ad hoc,” the lowest maturity level.

The City’s management officials stated that it had a zero-tolerance policy for fraud, which is an important step for the commitment to integrity and combatting fraud. However, the City had not taken key steps in creating an antifraud culture: The City did not (1) perform a preliminary assessment of the ESG CARES Act program to identify how vulnerable it was to fraud and the major types of fraud risks (determining fraud exposure), (2) promote fraud awareness throughout the departments involved with the ESG CARES Act program, such as required antifraud training for City employees and (3) have a dedicated antifraud component.

While the City had not performed an assessment of its vulnerability to fraud for the ESG CARES Act program, it had a policy team, comprised of senior-level management, that met weekly to discuss risks for its departments. For HUD-related projects, the meetings were focused on the risks of acquiring properties and the likelihood of projects’ being completed within the timeframes and the associated risks of not completing the project. The meetings also covered the potential fraud or ethical issues identified. However, these meetings did not involve assessments to identify the level of fraud for the City and programs that may be susceptible to fraud in order to implement an antifraud strategy.

Although there was no specific fraud training for employees who oversaw the ESG CARES Act program, the City did have other activities in place, such as ethics training required every 2 years for all employees, an employee code of conduct, and a form for disclosures of conflicts of interest. These activities helped to ensure the ethical integrity of City employees but did not help them identify or be aware of fraud committed by others doing business with the ESG CARES Act program. As noted in the Antifraud Playbook, promoting fraud awareness can be developed through training and is vital to a strong antifraud culture.

Although the City did not have a dedicated fraud department, function, or team, a division within the City (Internal Control Division) was responsible for conducting audits based on a risk-based audit plan and investigating complaints from the integrity hotline, through which City employees could report fraud. However, this division was not responsible for assessing fraud risks for the ESG CARES Act program or other City programs.

Phase 2 – identify and assess maturity level: The City did not perform a fraud risk assessment.

The Antifraud Playbook encourages organizations to identify fraud risks and develop a path forward for executing, repeating, and expanding a fraud risk assessment that is unique and customizable for the organization. Further, managers who effectively assess fraud risks attempt to fully consider the specific fraud risks the organization faces, analyze the potential likelihood and impact of fraud schemes, and then document prioritized fraud risks. Our assessment of the City’s maturity within this phase identified its status as “ad hoc,” the lowest maturity level.

The City had not identified fraud risks or developed a fraud risk assessment for its ESG CARES Act program. It was reactive to complaints of fraud and was not proactive in understanding its vulnerability

to fraud by identifying fraud risks and the likelihood and impact of those risks. For example, for the ESG CARES Act program, the City relied on reported fraud allegations. City officials stated that there had been no significant complaints related to fraud for the ESG CARES Act program so there had not been a need to focus efforts on antifraud activities. While there had been no recent known fraudulent activity for the ESG CARES Act program, there was fraudulent activity in 2017 for the City's ESG program, which receives annual funding from HUD.¹⁰ The City's Department of Community Services (DCS), which is involved in administering the ESG CARES Act program, also had fraudulent activity in 2020 for another program.¹¹ City officials stated that the issues they had been dealing with from the ESG CARES Act subrecipients were related more to mistakes or a difference in the interpretation of rules than to fraud.

Conducting a fraud risk assessment of the ESG CARES Act program would enable the City to identify specific fraud risks and fraud risk schemes, determine a fraud risk tolerance and develop an antifraud strategy to address the most significant fraud risks, and examine the suitability of existing controls in preventing fraud from occurring.

Phase 3 – prevent and detect maturity level: The City did not adequately implement antifraud controls to mitigate the risk of fraud.

The Antifraud Playbook encourages agencies to develop or strengthen antifraud controls that mitigate the highest risk areas and to start or advance a fraud analytics program. Managers who effectively manage fraud risks in this phase design and implement specific control activities, including policies, procedures, techniques, and mechanisms, to prevent and detect potential fraud. Our assessment of the City's maturity within this phase identified its status as "ad hoc," the lowest maturity level.

The City did not have (1) a data analytics tool to identify potential fraud,¹² (2) targeted antifraud training, or (3) a dedicated hotline for external entities to report potential fraud. The Antifraud Playbook states that the most effective antifraud control is a data analytics tool of some sort, which does not have to be costly or complex.

City officials stated that they did not have controls designed specifically for fraud but had some controls integrated into their standard operating procedures. Some of the fraud controls and activities in place for the ESG CARES Act program included the following:

- Three hotlines for individuals to report potential fraud: (1) the integrity hotline for City employees, (2) the Section 8 hotline, and (3) the Ethics Commission website for reporting ethical concerns. However, there was no hotline information on the City's main website or the DCS website for external entities to report potential ESG CARES Act program fraud. Also, the Section 8 hotline was included only on the division's website that oversees the Section 8 program (the

¹⁰ The fraudulent activity involved an employee of a City ESG subrecipient who used fake landlords and rental agreements from 2015 to 2017 to defraud the ESG program.

¹¹ A former DCS employee was hired in August 2020 as the CARES program administrator and accepted financial benefits from an applicant who filed fraudulent applications for CARES Act funds to influence the approval of the applications.

¹² While there was not a data analytics tool implemented for the ESG CARES Act program, the City had a tool in place for its Rental and Utility Relief Program, which was designed by the City's Department of Information Technology to validate addresses submitted by applicants and flag duplicate addresses used.

Community Assistance Division within DCS) and referred only to the Section 8 office. DCS officials stated that there were other reporting mechanisms for individuals to report potential fraud, which included the Office of the Mayor, the Office of the Auditor, and directly to DCS. However, there was no formal tracking system for these other reporting mechanisms, and DCS officials stated that it was up to each individual who received a complaint to track and follow up on the reported complaint. Without a tracking system, DCS could not ensure that allegations of fraud were followed up on, and it could not aggregate data or identify trends that could assist it in improving its fraud risk management practices.

- Review of all payment requests submitted by subrecipients: DCS primarily used subrecipients to implement activities for the ESG CARES Act program, and these subrecipients were required to submit monthly written requests for payment. The requests were required to include a certification that all information was accurate and complete and included supporting documentation, such as invoices and payroll reports. DCS reviewed the supporting documentation for eligibility before the payments were made. The payment requests included multiple levels of approval within DCS and were then forwarded to BFS for additional review and payment. However, the reviews focused on eligibility with the requirements and did not include reviewing for potential fraud schemes that would have been identified in phase 2 (identify and assess).
- A modified process for monitoring of ESG CARES Act subrecipients: DCS normally conducted site visits for the ESG program but had implemented monthly narratives due to the pandemic. These narratives included the activity completed for the month, challenges in meeting the grant activity, and a description of budget variances and were required to be submitted by subrecipients with the payment requests. DCS had not resumed onsite monitoring for the ESG CARES Act program; however, the Federal Project Monitoring unit, within BFS, had planned onsite monitoring for two ESG CARES Act recipients.

While the fraud controls and activities the City had in place for the ESG CARES Act was a good start, the Antifraud Playbook states that the most effective antifraud control is a data analytics tool of some sort. Establishing a robust fraud analytics effort will go from a “pay and chase” approach to a predictive approach to identify instances of potential fraud before they occur. The Association of Certified Fraud Examiners’ Report to the Nations found that organizations using data analytics techniques to fight fraud reduced the cost of fraud schemes by 52 percent and reduced the duration by 58 percent. Also, the City did not have targeted antifraud training or a dedicated hotline for external entities to report potential fraud, which contributed to the lowest maturity level for this phase.

Phase 4 – insight into action maturity level: The City did not have a process to monitor or evaluate the effectiveness of its fraud risk management activities.

The Antifraud Playbook encourages agencies to use available information, either within the agency or from external sources, and turning that insight into actionable tasks. Effective management in this phase would involve managers’ monitoring and evaluating the effectiveness of preventive activities, including a fraud risk assessment and antifraud strategy, as well as controls to detect fraud and response efforts. Our assessment of the City’s maturity within this phase identified its status as “ad hoc,” the lowest maturity level.

Without a formal fraud risk management framework in place, the City was not able to monitor and evaluate or enhance the effectiveness of preventive activities, such as fraud risk assessments, antifraud training, analytics activities, and antifraud controls. Simply put, the City could not monitor or evaluate a process that it had not yet designed or implemented.

The City Did Not Consider Implementing an Adequate Fraud Risk Management Framework

The City's overall fraud risk management was at the lowest maturity level because the City did not consider implementing an adequate fraud risk management framework due to a lack of fraudulent activity reported for the ESG program. However, without a fraud risk management framework in place, there was an increased risk of undetected and unreported fraud. The City considered that the controls it had in place were sufficient based on the lack of reported fraud.

The City departments involved with the oversight of the ESG CARES Act program did not follow either the Standards for Internal Control in the Federal Government (Green Book) or the COSO Internal Control Integrated Framework, which is recommended for non-Federal entities that receive Federal funds.¹³ The Green Book and COSO internal control frameworks both include principles to consider the potential for fraud when assessing risks. Due to the importance of this principle, both organizations have published fraud risk management guides with the intention to support organizations in meeting this principle. GAO and COSO make it clear that for a system of internal control to be effective, each of the principles must be present, functioning, and operating together in an integrated manner. If a principle or component is not effective or the components are not operating together in an integrated manner, an internal control system cannot be effective.

While there are no HUD regulations or other HUD requirements for the City to specifically implement a fraud risk management framework as described in the Framework and Playbook, regulations at 2 CFR 200.303 state that grantees must establish internal controls which should comply with the Green Book or COSO. Green Book and COSO state that assessing the risk of fraud is one of many principles for establishing an effective internal control system. We also noted in a prior HUD, Office of Inspector General (OIG), audit report¹⁴ that HUD stated that the responsibility for the assessment and mitigation of fraud risks rested primarily with the grantees for the CDBG and ESG programs. Further, Office of Management and Budget Circular A-123 states that "the Federal Government has a number of complex inter-dependencies with State and local governments, and other recipients of Federal funding. From an ERM (enterprise risk management) perspective, these inter-dependencies called the 'extended enterprise' impacts the Agency's risk management, and give rise to certain additional risks, which need to be considered in the Agency's risk profile." Without the requirement of a framework, HUD and the City are missing a critical control that could identify, assess, and mitigate fraud risks for more than \$25 million in ESG CARES Act funding allocated to the City. Therefore, it is in the City's best interest to improve its

¹³ Regulations at 2 CFR 200.303 state that the non-Federal entity must establish and maintain effective internal control over the Federal award that provides reasonable assurance that the non-Federal entity is managing the Federal award in compliance with Federal statutes, regulations, and terms and conditions of the Federal award. These internal controls should comply with guidance in Standards for Internal Control in the Federal Government, issued by the Comptroller General of the United States, or the Internal Control Integrated Framework, issued by COSO.

¹⁴ HUD OIG Audit Report 2022-FO-0801, Fraud Risk Inventory for the CDBG and ESG CARES Act Funds, issued October 12, 2021

fraud risk management practices for the ESG CARES Act program to better protect funds from waste, fraud, and abuse.

Conclusion

The influx of funding (\$25.6 million) that the City received for its ESG CARES Act program from the CARES Act to respond to the COVID-19 pandemic increased the risk of fraud. As the grantee, the City is responsible for ensuring that grant funds are used in accordance with program requirements, and it is prudent for the City to incorporate fraud risk management practices that proactively identify and respond to fraud risks and safeguard taxpayer funds. Although the City had implemented some fraud controls and activities for the ESG CARES Act program, the maturity level of its fraud risk management practices was at the lowest level – ad hoc. Due to having the lowest maturity level, the City missed opportunities to reduce the risk of losses to fraud. The City could improve its fraud risk management practices, such as create an antifraud entity, communicate fraud awareness to its departments, regularly conduct fraud risk assessments, consider the development of data analytics tools to identify potential fraud, develop a hotline for external entities to report fraud, create a tool to track allegations of fraud, and develop a response plan to address identified fraud risks by implementing antifraud risk management controls and activities to constantly adapt and improve them. Because the City did not consider it necessary to implement an adequate fraud risk management framework due to the lack of known fraudulent activity and HUD’s not requiring a framework, more than \$25 million in ESG CARES Act funds administered by the City will continue to be at a greater risk of fraud. Even though we are now operating in a post pandemic environment, the increased risk of fraud will remain until the City creates a culture and framework that can regularly detect and prevent fraud, as well as identify, assess, and take corrective action on fraud risks.

According to the Association of Certified Fraud Examiners: “One reason we can likely expect more fraud to proliferate is the massive changes in underlying fraud risks that have arisen since the onset of the pandemic...business leaders need to treat these changes as more than temporary and incorporate them into their risk assessments and anti-fraud plans.”

Recommendations

We recommend that the Director of HUD’s Honolulu Office of Community Planning and Development instruct the City to

- 1A. Improve or enhance its antifraud efforts for the ESG program and incorporate fraud risk management practices that are consistent with the best practices identified in the Government Accountability Office’s A Framework for Managing Fraud Risks in Federal Programs and Chief Financial Officers Council and Treasury Bureau of the Fiscal Services’ Antifraud Playbook.
- 1B. Obtain training or technical assistance as needed on the implementation of fraud risk management practices.

Scope and Methodology

We conducted the audit offsite from July through December 2023. Our audit covered the period April 1, 2020, to June 30, 2023. All interviews and discussions were conducted offsite. Our audit focused on the City's fraud risk management practices for the ESG CARES Act grant funds.

To gain an understanding of the fraud risk management environment at the City and adequately conduct our assessment, we performed the following:

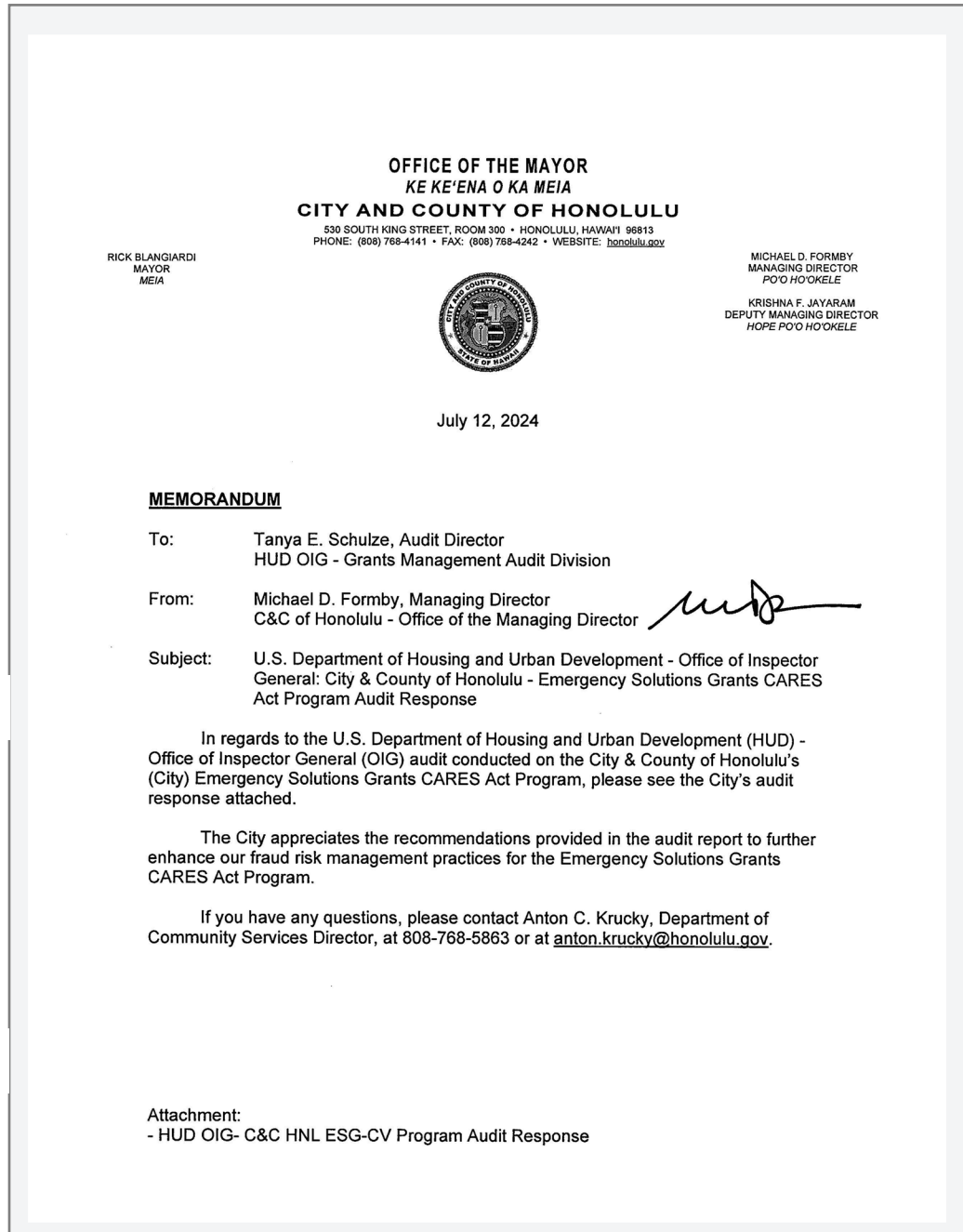
- Reviewed pertinent fraud risk guidance and criteria, including GAO's Standards for Internal Control in the Federal Government, COSO's Internal Control Integrated Framework, CFOC and Treasury BFS's Antifraud Playbook, and GAO's A Framework for Managing Fraud Risks in Federal Programs.
- Interviewed officials from the City and the HUD Honolulu field office.
- Reviewed City policies and procedures, as well as other relevant documentation.
- To determine the maturity level of the City's fraud risk management practices, we used the Antifraud Program Maturity Model contained in the Antifraud Playbook. We followed GAO's A Framework for Managing Fraud Risks in Federal Programs and CFOC and Treasury BFS's Antifraud Playbook guidance to perform our assessment and identify areas for improvement.

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

Appendixes

Appendix A – Auditee and HUD Comments and OIG’s Evaluation Ref to OIG Evaluation – Auditee Comments

The following comments were provided by the City and County of Honolulu:



Ref to OIG Evaluation – Auditee Comments

 **Comment 1 >**

U.S. Department of Housing and Urban Development - Office of Inspector General:
City & County of Honolulu - Emergency Solutions Grants CARES Act Program Audit Response

The U.S. Department of Housing and Urban Development (HUD), Emergency Solutions Grant Coronavirus Aid, Relief, and Economic Security Act (ESG-CV) award to the City and County of Honolulu (City), that was administered by the Department of Community Services (DCS), was critical in the City's response to safeguard this particularly vulnerable segment of O'ahu's population.

The City was aware of the magnitude of its award relative to its annual formula award and believes that the controls implemented to administer the award were appropriate given the exigent nature of the coronavirus crisis and the timeline provided to fully expend the funding. With the ESG-CV funding the City was immediately able to implement a variety of programs to prevent, prepare for, and respond to the coronavirus, among individuals and families who are experiencing homelessness or at risk of becoming homeless by mitigating the impacts caused by coronavirus.

 **Comment 2 >**

Where creative solutions were necessary to manage this unprecedented circumstances, the City did its best to maintain its internal controls to the extent practicable relative to its federal grants programs. The following guidelines, policies, and procedures were developed:

- Emergency Solutions Grants CoronaVirus Guidebook (ESG-CV)
 - a. Program Standards
 - b. Recordkeeping Standards
- Standard Operating Procedures – ESG CV
- Community Based Development Division Fraud Controls

Each of these items included control activities and monitoring to allow for the proper review and escalation to senior and executive levels of management for any perceived anomalies or improprieties.

Responding to the coronavirus otherwise required a great deal of ingenuity to ensure the safety and well-being of those experiencing homelessness or at risk of homelessness. Using ESG-CV funds the City was able to respond appropriately to the coronavirus including a number of innovative and successful programs including:

1. Creating new and alternative shelter and supportive housing to respond to the reduction in congregate shelter capacity due to coronavirus restrictions to house those experiencing homelessness, or at risk of homelessness.
2. Investing in building improvements to mitigate the spread of coronavirus in facilities that service ESG populations and mitigate the impact of coronavirus restrictions.
3. Distributing vaccines and other health care services.
4. Increased homelessness prevention activities associated with the negative economic impact of coronavirus.
5. Increasing access to hygiene facilities and products to prevent the spread of coronavirus.
6. Expanding outreach and education to homeless populations including those with special needs.

 **Comment 3 >**

Relative to this monitoring report, DCS acknowledges the recommendations of the monitoring report to improve its internal controls and control environment as it relates to fraud. DCS will be

 **Comment 3 >**

U.S. Department of Housing and Urban Development - Office of Inspector General:
City & County of Honolulu - Emergency Solutions Grants CARES Act Program Audit Response

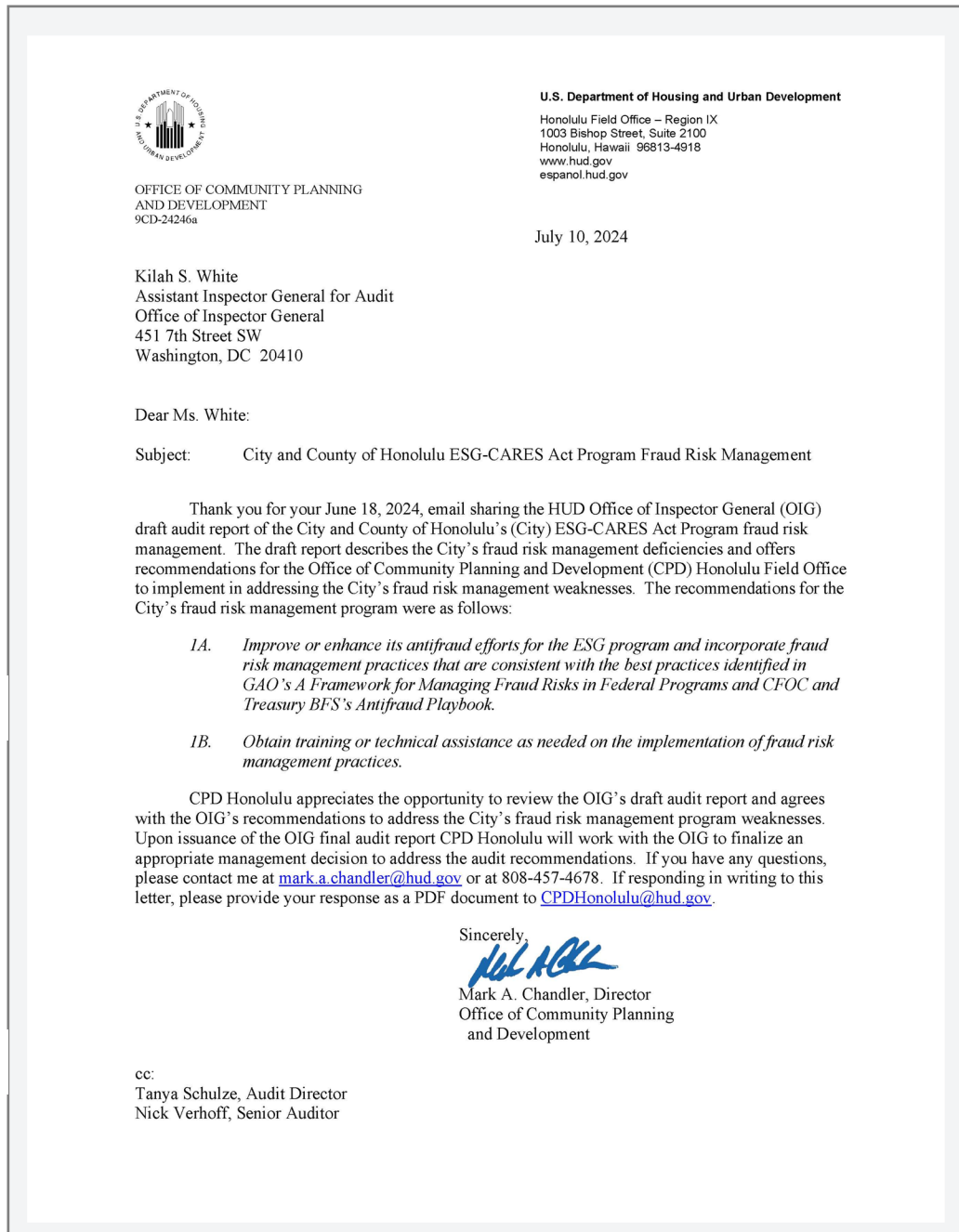
working to implement and incorporate further internal controls as recommended in the monitoring report, specific to preventing fraud, taking measures identified in the –

1. U.S. Government Accountability Office – A Framework for Managing Fraud in Federal Programs; and
2. CFO Council Anti-Fraud Playbook (Playbook).

We have found both resources helpful to enhance DCS' approach mitigating the risk of fraud in a form that best suits City operations including the Fraud Risk Scoring and Playbook Mapping tools. DCS staff will be looking for opportunities for training and technical assistance to further enhance the development of a more robust fraud framework and tools to mitigate the risk of fraud for the federal programs that it administers. DCS is also committed to working within the City to integrate these practices into the City's larger framework to address fraud.

Going forward with new grant awards, DCS intends to implement tools like the Fraud Risk Map from the Playbook to document fraud assessment and its response to any fraud risks identified therein for further monitoring over the life of the grant at the individual program or contract level as applicable. DCS will also use this tool to retrospectively evaluate its program-level approach to manage fraud risk – as needed to address changing circumstances or at the end of each grant.

The following comments were provided by the HUD Honolulu CPD Director:



 **Comment 4 >**

OIG Evaluation of Auditee and HUD Comments

- Comment 1 The City and County of Honolulu (City) said it believes the controls implemented to administer the ESG CARES Act award were appropriate given the exigent nature of the coronavirus crisis and the timeline to fully expend the funding. We recognize the challenges that grantees faced during the pandemic and the ways in which grantees had to adapt to a changing and difficult operating environment.
- The fraud risk management framework is a broader entity-wide concept. As noted in the audit report, grantees should not only consider fraud risk management practices for pandemic funding, but also consider these best practices portfolio wide since grantees receive Federal funds from HUD as well as other Federal agencies. The focus of this audit was for the ESG CARES Act program, so we only reported on the fraud risk management framework for this program.
- Comment 2 The City said it did its best to maintain its internal controls to the extent practicable relative to its federal grants programs and developed guidelines, policies, and procedures. These internal controls, guidelines, policies, and procedures were reviewed as part of the audit and, where applicable, we note some of the fraud controls and activities that were in place for the ESG CARES Act program.
- Comment 3 We commend the City for its willingness to address the audit report recommendations, and to use both the CFOC Antifraud Playbook and GAO Framework as it enhances its antifraud activities and controls such as a Fraud Risk Map. We look forward to working with CPD and the City during the audit resolution process to implement the recommendations.
- Comment 4 We appreciate HUD's cooperation and agreement with the recommendations. We look forward to working with HUD during audit resolution.