SUMMARY REPORT DIGEST

ILLINOIS HOUSING DEVELOPMENT AUTHORITY

Financial Audit
For the Year Ended June 30, 2018

Release Date: January 29, 2019

FINDINGS THIS AUDIT: 3

	New	Repeat	Total
Category 1:	**1**	**1**	**2**
Category 2:	**0**	**1**	**1**
Category 3:	**0**	**0**	**0**
TOTAL	**1**	**2**	**3**

FINDINGS LAST AUDIT: 2

AGING SCHEDULE OF REPEATED FINDINGS

Repeated Since	Category 1	Category 2	Category 3
2015		**18-3**	
2014	**18-1**		

INTRODUCTION

This digest covers the Illinois Housing Development Authority (Authority) Financial Audit as of and for the year ended June 30, 2018. The Authority's Compliance Examination (including the Single Audit) covering the year ended June 30, 2018 will be issued in a separate report at a later date.

SYNOPSIS

- **(18-1)** The Authority was unable to support the historical detail assumptions used in its allowance for loan loss calculation for the multi-family loan programs. Additionally, the Authority has not established adequate internal controls for ensuring the allowance for loan loss is properly calculated and presented in its financial statements.

- **(18-2)** The Authority has not established adequate internal controls over the financial reporting of investments, including recording the fair market value of certain investments, properly classifying investments as current vs. noncurrent, and properly reporting investment activity within the statement of cash flows.

- **(18-3)** The Authority has not established adequate internal controls over the financial reporting process, including the preparation of program loans receivable footnote disclosures and recording revenue and expense transactions within the Hardest Hit Fund.

Category 1: Findings that are **material weaknesses** in internal control and/or a **qualification** on compliance with State laws and regulations (material noncompliance).

Category 2: Findings that are **significant deficiencies** in internal control and **noncompliance** with State laws and regulations.

Category 3: Findings that have **no internal control issues but are in noncompliance** with State laws and regulations.

{Financial information is summarized on next page.}

ILLINOIS HOUSING DEVELOPMENT AUTHORITY
FINANCIAL AUDIT
For the Year Ended June 30, 2018

FINANCIAL POSITION - ALL FUNDS	2018	2017
Assets		
Cash and investments - unrestricted	$ 763,043,850	$ 746,499,987
Investments - restricted	709,126,352	745,588,980
Net Program loans receivable	1,215,019,862	1,306,871,453
Other	188,072,447	176,593,285
Total	2,875,262,511	2,975,553,705
Deferred Outflows of Resources	523,772	688,821
Liabilities		
Bonds and Notes Payable	1,164,424,724	1,147,673,217
Due to State of Illinois	324,010,464	340,321,548
Deposits held in escrow	139,757,584	141,574,862
Other	122,361,002	131,911,001
Total	1,750,553,774	1,761,480,628
Deferred Inflows of Resources	5,145,477	8,278,172
Net Position		
Net investment in capital assets	2,591,337	273,370
Restricted	887,322,089	1,001,365,319
Unrestricted	230,173,606	204,845,037
Total	$ 1,120,087,032	$ 1,206,483,726

ADMINISTRATIVE FUND OPERATIONS	2018	2017
Revenues		
Service Fees	$ 8,364,853	$ 9,234,024
Interest and investment income	29,161,392	30,629,303
Federal assistance programs	79,877,059	97,716,978
Other	21,299,132	17,611,636
Total	138,702,436	155,191,941
Expenses		
Salaries and benefits	19,970,427	18,847,698
Professional fees	2,349,129	1,840,593
Other general and administrative	2,677,724	1,735,059
Transfers, net	1,722,650	5,239,999
Financing Costs	503,859	751,585
Federal assistance programs	79,877,059	97,716,978
Provision for est. loss on loan receivable	1,638,493	1,757,569
Other	3,234,998	141,538
Total	111,974,339	128,031,019
Change in net position	$ 26,728,097	$ 27,160,922

EXECUTIVE DIRECTOR
During Engagement: Audra A. Hamernik Current: Audra A. Hamernik

FINDINGS, CONCLUSIONS, AND RECOMMENDATIONS

INADEQUATE ALLOWANCE FOR LOAN LOSS METHODOLOGY AND LOAN RATING REVIEW PROCESS

Controls over the allowance for loan loss need improvement

The Authority was unable to support the historical detail assumptions used in its allowance for loan loss calculation for the multi-family loan programs. Additionally, the Authority has not established adequate internal controls for ensuring the allowance for loan loss is properly calculated and presented in its financial statements.

During our audit, we reviewed the allowance for loan loss methodology for the multi-family loan program and noted the Authority could not produce an analysis supporting the rationale for its calculation of the loan loss reserve factors (probability of default and expected loss) that are used in its allowance for loan loss calculation.

Back-testing of the allowance was not performed

The Authority has not documented how the loan loss reserve factors for the multi-family loan programs have been historically calculated and over what period the probability of default is measured. Further, the Authority did not perform back-testing (typically performed on at least an annual basis) on its allowance for loan loss estimates for the multi-family loan programs to determine whether the allowance for loan loss produces estimates that have been historically sufficient to cover incurred losses over a period of time that aligns with the period used to estimate the probability of default values.

Furthermore, during our testing of 43 multi-family loan relationships risk ratings (66 loans) as of June 30, 2018, we noted differences in the ratings determined by the Authority on their loan rating scale compared to our independent ratings determined during our review.

We found the Authority's risk ratings to be reasonable on 28 of the 43 relationships (46 of the 66 loans) and we found the Authority's risk ratings to be unreasonable for 15 of the 43 relationships (20 of the 66 loans).

Some of the differences in loan ratings are as follows:

Housing Trust Fund loans were under reserved by $11,968,248

- 4 differences in Housing Trust Fund loan ratings resulted in an under reserve of $331,510 for the Illinois Affordable Housing Trust Fund. In response to this finding, the Authority reviewed the total population of Housing Trust Fund loans and determined they were under reserved by a total of $11,968,248. A proposed adjustment for this difference was recorded by the Authority.

HOME Program Fund loans were under reserved by $9,735,868

- 7 differences in HOME loan ratings resulted in an under reserve of $2,077,978 for the HOME Program Fund. In response to this finding, the Authority reviewed the total population of HOME Program loans and determined they were under reserved by a total of $9,735,868. A proposed adjustment for this difference was recorded by the Authority.

Nonmajor Governmental Funds loans were under reserved by $4,361,501

- Five differences in Nonmajor governmental fund loan ratings resulted in an under reserve of $2,322,997 for the Nonmajor Governmental Funds. In response to this finding, the Authority reviewed the total population of Nonmajor Governmental Fund loans and determined they were under reserved by a total of $4,361,501. A proposed adjustment for these differences was recorded by the Authority.

Additionally, in response to the differences noted above, the Authority reviewed the total population of Administrative Fund loans and determined they were under reserved by $754,928. A proposed adjustment for this difference was recorded by the Authority. (Finding 1, pages 81-83) **This finding has been repeated since 2014**

We recommended the Authority review its current policies and procedures to ensure the assumptions used in the allowance for loan loss calculation are appropriate and that loan ratings are calculated appropriately.

Authority agrees with auditors

Authority officials accepted the recommendation. *(For the previous Authority response, see Digest Footnote #1.)*

INACCURATE FINANCIAL REPORTING

The Illinois Housing Development Authority (Authority) has not established adequate internal controls over the financial reporting process of investments, including recording the fair market value of certain investments, properly classifying investments as current vs. noncurrent, and properly reporting investment activity within the statement of cash flows.

Authority did not accurately record the fair market value of its discount note investment securities

During our audit of the financial statements as of June 30, 2018, we noted the Authority did not correctly record the fair market value for 18 of its discount note investment securities. As a result, the Authority's investment securities were understated by $173,723 within the Administrative Fund, $838,001 within the Mortgage Loan Program Fund, and $1,522,989 within the Single Family Loan Program Fund. A proposed adjustment for these differences was recorded by the Authority.

In addition, we noted the Authority improperly classified its investments as follows:

The Authority misclassified its investments

- Current and noncurrent investments within the Rental Housing Support Program Fund were improperly classified, resulting in a difference of $27,528,386 in each category.
- Current and noncurrent investments within the Administrative Fund were improperly classified, resulting in a difference of $222,451,738 in each category.
- Current and noncurrent restricted investments within the Administrative Fund were improperly classified, resulting in a difference of $24,785,338 in each category.
- Current and noncurrent restricted investments within the Mortgage Loan Program Fund were improperly classified, resulting in a difference of $66,452,197 in each category.
- Current and noncurrent restricted investments within the Single Family Loan Program Fund were improperly classified, resulting in a difference of $98,013,824 in each category.

A proposed adjustment for these reclassifications was recorded by the Authority.

The Authority's Statement of Cash Flows required numerous adjustments

In addition, we noted the Authority improperly reported investment purchases, proceeds from sales, and interest received on investments within the net cash provided by (used in) investing activities section of the statement of cash flows for the Administrative Fund, Mortgage Loan Program Fund, and Single Family Program Fund. A proposed adjustment for these differences was recorded by the Authority. (Finding 2, pages 84-87)

We recommended the Authority review its current internal control policies and procedures to ensure investments are properly valued and classified in the general ledger and the financial statements, and to ensure investment activity is properly reported and presented in the financial statements.

Authority agrees with auditors

Authority officials accepted the recommendation.

INACCURATE FINANCIAL REPORTING

The Authority's Program Loan Receivable footnote was not properly presented

The Illinois Housing Development Authority (Authority) has not established adequate internal controls over the financial reporting process, including the preparation of program loans receivable footnote disclosures and recording revenue and expense transactions within the Hardest Hit Fund.

During our audit of the financial statements as of June 30, 2018, we noted the following:

Disbursements and repayments incorrectly reported

- The Authority incorrectly reported program loans receivable disbursements and repayments within footnote 5 of the financial statements for the Mortgage Loan Program Fund (MLP) and Single Family Program Fund (SFP). The disbursements and repayments were incorrectly reported by $84,000 in the MLP and $3,807,000 in the SFP. A proposed adjustment for these reclassifications was recorded by the Authority.

Scheduled receipts of principal on gross program loans receivable misreported in the Authority's footnote for the Illinois Affordable Housing Trust Fund, HOME Program Fund, and Authority proprietary funds

- The Authority incorrectly reported scheduled receipts of principal on gross program loans receivable in the Illinois Affordable Housing Trust Fund in the fiscal years subsequent to June 30, 2018 and thereafter, within footnote 5 of the financial statements, with differences ranging from $41,000 to ($210,000). A proposed adjustment for these reclassifications was not recorded by the Authority.

- The Authority incorrectly reported scheduled receipts of principal on gross program loans receivable in the HOME Program Fund in the fiscal years subsequent to June 30, 2018 and thereafter, within footnote 5 of the financial statements, differences ranging from $19,000 to ($165,000). A proposed adjustment for these reclassifications was not recorded by the Authority.

- The Authority incorrectly reported scheduled receipts of principal on gross program loans receivable in the proprietary funds in the fiscal years subsequent to June 30, 2018 and thereafter, within footnote 5 of the financial statements, with differences ranging from ($9,000) to $540,000. A proposed adjustment for these reclassifications was not recorded by the Authority.

In addition, we noted the U.S. Department of Treasury conducted a review of the prior year Hardest Hit Fund activities and determined that $885,069 of expenses were improperly charged to the Hardest Hit Fund. In response to this review, the Authority improperly recorded an increase to Other Revenue within the Hardest Hit Fund instead of a decrease to General and Administrative expenditures.

As a result, Other Revenue and General and Administrative expenditures were overstated by $765,228 within the Hardest Hit Fund. A proposed adjustment for this difference was recorded by the Authority.

In addition, Other Revenue and General and Administrative expenditures were overstated by $119,841 within the Hardest Hit Fund. A proposed adjustment for this difference was not recorded by the Authority. (Finding 3, pages 88-90) **This finding has been repeated since 2015.**

We recommended the Authority review its current internal control policies and procedures to ensure financial transactions are accurately reported in the general ledger and the financial statements, including footnote disclosures.

Authority agreed with auditors

Authority officials accepted the recommendation. *(For the previous Authority response, see Digest Footnote #2.)*

AUDITOR'S OPINION

Our auditors stated the financial statements of the Authority as of June 30, 2018, and for the year then ended, are fairly stated in all material respects.

The financial audit was conducted by KPMG LLP.

SIGNED ORIGINAL ON FILE

JANE CLARK
Division Director

This report is transmitted in accordance with Section 3-14 of the Illinois State Auditing Act.

SIGNED ORIGINAL ON FILE

FRANK J. MAUTINO
Auditor General

FJM:TLK

DIGEST FOOTNOTES

#1 – Need To Improve Controls Over The Allowance For Loan Loss

The Authority will continue to perform back testing to further support the assumptions used in the allowance for loan loss calculation. In addition, review of current policies, procedures, and controls will be completed to ensure assumptions are applied accurately and that ratings are adequately supported.

The Authority notes the new loan loss reserve policy adopted by the Board of Directors was based on an analysis of actual losses incurred from June 30, 2002 to June 30, 2017. That analysis showed the multifamily loan portfolio had experienced 50 losses with an average aggregate write-off of approximately $1.7 million per year (or 0.13% of the portfolio). The Authority's fiscal year 2017 estimated loan loss for the $1.2 billion multifamily portfolio was approximately $34 million (or 2.6% of the portfolio).

#2– Inaccurate Financial Reporting

The Authority will review the classifications for all current and non-current liabilities to ensure proper reporting. Additionally, the Authority made the appropriate change to the internal policies and procedures to adhere to GAAP.