The original documents are located in Box 65, folder "FY 1978 Director's Review - HUD (2)" of the James M. Cannon Files at the Gerald R. Ford Presidential Library.

#3. PUBLIC HOUSING

Issue Paper
Department of Housing and Urban Development
1978 Budget
Issue #3: Public Housing

SUBISSUE A: Operating Subsidies

Background

In FY 1977, approximately 1,182,000 low-income families will reside in public housing owned by local housing authorities (LHAs). In addition to paying for all construction/acquisition costs for these projects, HUD also provides operating subsidies for about 80 percent of the units. The number of units receiving an operating subsidy and the total cost of that subsidy have increased steadily since 1969. The number of units subsidized has increased 80 percent from 1969 to 1976. The total subsidy costs have increased from $12.6 million in 1969 to $535 million in 1976.

HUD currently estimates operating subsidy requirements using the Performance Funding System (PFS) to develop operating costs for "well-run" LHA public housing projects and a separate revenue forecast which inflates actual receipts in a base year with a 3 percent factor. In the FY 1977 Budget, the Administration proposed a new revenue standard which assumed larger rental payments by public housing tenants. Congress did not approve the change, and HUD does not propose resubmitting the request. HUD has proposed changes in the current PFS formula, however, and these are reflected in its budget submission.

Subissue A-1 - Revenue Standard

Should rental income estimates under the PFS be increased to equalize the rent burden between low-income tenants in public housing and in publicly assisted private housing (section 8)?

Alternatives

#1. Continue the lower rent standard for public housing tenants (HUD request).

#2. Establish a public housing rent standard equal to 25 percent of adjusted income, as defined under public housing (OMB recommendation).

#3. Establish a public housing rent standard equal to 25 percent of adjusted income, as defined under section 8.

Analysis

Budget Authority/Outlays ($ in millions)	1976 BA	1976 O	1977 BA	1977 O	1978 BA	1978 O	1979 BA	1979 O	1980 BA	1980 O	1981 BA	1981 O	1982 BA	1982 O
Current policy (Alt. #1 HUD request)	535	508	611	542	719	618	848	765	990	901	1116	1036	1230	1156
Change from current policy:														
Alt. #2 (OMB recom.)	---	---	---	---	-116	-116	-120	-120	-123	-123	-127	-127	-132	-132
Alt. #3	---	---	---	---	-176	-176	-182	-182	-186	-186	-192	-192	-199	-199

Under current law, LHAs are permitted to establish their own rental levels within the general restriction that rent cannot exceed 25 percent of adjusted income. In effect, the current PFS has no rental standard. HUD's budget estimates merely assume that LHA rental income will represent about 21 percent of tenant adjusted income, or about 17 percent of gross tenant income. Since the amount of Federal operating subsidy provided depends on the difference between the PFS formula-determined operating cost standard and estimated rental receipts, the current system perversely encourages those LHAs with low-rent levels and penalizes those with high rent levels.

The public housing standard differs from the section 8 standard in two ways. First, the rental standard for section 8 requires tenants to pay 25 percent of their adjusted income toward the unit rental, with the Government providing the difference between that amount and the unit's fair market rent. Second, fewer deductions from gross income are permitted under section 8, compared with public housing definitions. Consequently, under section 8 definitions, adjusted income is about 12 percent greater than under public housing definitions. The adjustments to income are defined by law and the public housing adjustments are compared with the section 8 adjustments in the table below.

Adjustments to Gross Income

Public Housing	Section 8
. $300 Deduction per minor dependent.	. $300 deduction per minor dependent.
. 5 Percent of family gross income (10 percent for elderly).	
. First $300 of spouse's income.	

Since HUD surveys indicate that public housing tenants differ in few respects from low-income families served under the section 8 rental assistance program, no fundamental social objectives are served by providing a differential rent burden between these two low-income tenant groups. Rather, a serious inequity between these two comparable renter groups exists.

The change in standards will impose a substantial one-time rent increase in 1978 of 20 percent for Alternative #2 and 24 percent for Alternative #3. Actual rental increases will vary, depending upon the current rent burden for each family.

Pros

- Would establish equity in rent burden between comparable low-income groups.
- Would reduce operating subsidy outlays.
- Would remove current PFS perverse incentives for rental efforts.

Cons

- Impose substantial 1-year rent increase for those tenant families currently bearing the lowest rent burden.
- Congress was unreceptive to similar proposal last year. However, legislation is required only to change the definition of adjusted income.

HUD Request: Alternative #1.

OMB Recommendation: Alternative #2. Although Alternative #3 will establish total consistency between public housing and section 8 tenants, Alternative #2 does not require new legislation and removes the most significant part of the current differential.

SUBISSUE A2

Statement of Issue

Should the inflation factor for tenant income (currently, 3 percent) be increased?

Analysis

Despite the similarities in the tenant groups served by section 8 and public housing, HUD forecasts a lower (3 percent) income growth for public housing tenants than for section 8 tenants (5 percent). The following table compares median incomes and the sources of income for these two tenant groups.

	Median Income	Income Sources (in percent)			
		Wages	AFDC	Other Welfare	Other
Public Housing	4,617	N/A	N/A	N/A	N/A
Section 8	4,198*	22	26	27	25

* Average.

The growth in median adjusted family income for public housing tenants from September 1971 to March 1976 increased at an average annual rate of 12.5 percent for elderly and 2.8 percent for nonelderly tenants. Since September 1974, however, nonelderly tenant adjusted income has increased 3.5 percent. Since elderly tenants occupy 43 percent of the units receiving operating subsidies, the weighted average annual increase in tenant income is 6.97 percent.

The additional rental income derived from the increase in income growth assumption (to 5 percent) is shown in the table below:

Additional Rental Income
($ in millions)

	1978	1979	1980	1981	1982
20 Percent rent standard........	30	46	65	84	105
25 Percent rent standard........	34	53	75	97	120

Pros

. Establish consistent income growth assumptions for comparable tenant groups.

. Reduces operating subsidy requirements and thus provides additional outlay savings.

. Is consistent with past growth in the weighted average of public housing tenant income.

Con

. 3 Percent growth is consistent with past average growth in public housing tenant income for nonelderly tenants.

. Use of the higher estimate could provoke Congress to eliminate the PFS altogether, thereby removing whatever control this system imposes on operating subsidies.

HUD Request: Continue to project tenant income growth at 3 percent per year.

OMB Recommendation: Project tenant income growth at 5 percent.

SUBISSUE A3: Operating Cost Standards

Statement of Issue

Should the current PFS estimating procedures for developing public housing operating cost standards be modified?

Alterantives

#1. Make no changes in current procedures (OMB recommendation).

#2. Change the variables in the basic formula and increase the inflation adjustment to 6 percent per year beyond 1977 (HUD request).

#3. Make no change in the basic formula variables, but adjust the inflation factor.

Analysis

Budget Authority/Outlays	1976		1977		1978		1979		1980		1981		1982	
($ in millions)	BA	O	BA	O	BA	O	BA	O	BA	O	BA	O	BA	O
Current policy														
Alt. #1 (OMB rec.)	535	508	576	527	683	583	812	729	953	865	1079	999	1192	1119
Change from current policy:														
Alt. #2 (HUD req.)	---	---	+35	+15	+36	+35	+36	+36	+37	+36	+37	+37	+38	+37
Alt. #3	---	---	+18	+5	+19	+18	+19	+19	+20	+19	+20	+20	+21	+20

HUD has developed a formula for determining operating cost standards for all LHA public housing projects, based on the average operating expenses of a separately determined set of "well-managed" projects in a base year. The specific variables included in the formula and their mathematical weights are determined solely by how well they predict the actual operating expenses of the "well-managed" projects for the specific base year. If, in subsequent years, the formula underestimates actual operating expenses for "well-managed" units, HUD changes the variables and/or their mathematical weights to improve their predictive accuracy.

HUD uses the formula to estimate an allowable cost increase for each project, assuming it were "well-managed." This increment is added to the operating cost allowed in the previous year and the revised total is then adjusted by an inflation factor to determine the next year's operating costs. The inflation factor used in HUD's 1978 budget submission assume 6 percent per year beyond 1977. Three points are relevant:

. The HUD-assumed inflation rate reflects mostly wage increases, since utility costs are currently excluded from the operating cost formula.

. The HUD rate exceeds currently anticipated inflation rates of 5 percent per year beyond 1977.

. There is no provision for productivity improvement.

The current 3 percent factor is consistent with currently anticipated inflation rates beyond 1977, allowing for a modest 2 percent per year productivity improvement.

The HUD procedure of annually revising the structure of the cost formula raises serious questions about the utility of this PFS approach.

. A meaningful and accurate cost standard should be relatively stable over time to evaluate the cost performance of LHA public housing projects.

. Estimating errors should raise questions about the actual cost performance of "well-managed" projects; instead, only the adequacy of the formula itself is questioned.

. If the formula is not a good predictor of a "well-managed" project's cost, its reliability for establishing a cost standard for other projects is moot.

. If the formula must be changed annually, its value for establishing budget year and outyear operating cost projections is highly suspect.

. An asymmetry problem exists since there is no way of recapturing excess allocations if a "well-managed" project's costs fall short of expectations.

Given this apparent degree of instability and given the lack of any incentives for those projects defined to be "well-managed" to increase their efficiency, OMB staff believe HUD and OMB should undertake a joint evaluation of the operation of the PFS next year.

Pros and Cons for Changing Formula Variables

Pro

. Revised formula improves prediction of "well-managed" project operating costs in new base year.

Cons

. Reason for prediction error may be poor definition of "well-managed" projects or inadequate cost performance by some of those projects deemed "well-managed."

. Continual changes in formula limit utility of formula approach for either controlling cost growth or evaluating cost performance of LHAs.

Pros and Cons for Adjusting Inflation Factor

Pros

. Previous 3 percent adjustment was not realistic.

. Provides measure of actual operating expenses, assuming current procedures and management efficiency continue.

Cons

. HUD's proposed factor more than fully funds anticipated inflation.

. Budgeting for full inflation adjustment eliminates any fiscal constraint requiring greater efforts to increase productivity and efficiency.

. HUD's procedure may double count inflation by first accounting for inflation in the incremental costs for well-managed units and then adding an additional inflation factor on top.

HUD Request: Alternative #2. HUD has demonstrated the "statistical superiority" of the revised formula for the new base year estimates. HUD staff acknowledge the lack of incentives for productivity improvement among those "well-managed" LHAs determining the current cost standards. However, HUD's primary concern is to make the operating costs of those other, "poorly managed," LHAs conform more closely to actual operating costs of "well-managed" projects.

OMB Recommendation: Alternative #1. A formula-determined cost standard that changes annually because the formula changes has little value as a cost standard. More evaluation is needed to determine (a) the reasons for prediction errors from a given formula, and (b) a theoretically sound formula which is relatively stable over time. However, the current procedure should be corrected now to provide some motivation (e.g., fiscal necessity) for improving the efficiency of the "well-managed" group of LHAs and those other LHAs whose cost performance is now consistent with the "well-managed" standard. About 50 percent of all LHA public housing projects are included in these last two categories. This alternative would deny HUD's request for a $35 million 1977 supplemental.

SUBISSUE B: Public Housing Project Note Sales to the Federal Financing Bank

Statement of Issue:

Should HUD sell long-term public housing project bonds to the Federal Financing Bank (FFB)?

Background

Under the public housing program, local housing authorities (LHAs) are responsible for financing the development or acquisition of LHA-owned projects. They issue tax-exempt notes during the construction stage, pledging their annual contributions contract with HUD (which provides for full amortization of the debt) as security. In the past, LHAs have replaced these notes with tax-exempt bonds when the projects were complete (or following acquisition). This financial arrangement is tantamount to a Federal guarantee of the tax-exempt LHA obligations. Without such pledges, the LHA obligations would be unsaleable. HUD also serves as marketing agent for the LHA obligations.

Because of market conditions on the long-term tax-exempt market, and at the advice of Treasury, HUD has not converted any project notes to long-term project bonds since 1974. The result is a continuous process of rolling over notes with a term of 1 year or less.

As of September 30, 1976, an estimated $5.3 billion of public housing notes were outstanding. This volume had been expected to decline in future years as permanent financing replaced the notes. However, congressional action in the Housing Authorization Act of 1976 (P.L. 94-375) mandated a resumption of public housing construction. The 1977 Appropriations Act for HUD provided $155 million of annual contract authority ($5.535 billion in budget authority) for new public housing.

Alternatives

#1. Continue to roll-over short-term project notes on the tax-exempt market.

#2. Sell long-term project bonds on the tax-exempt market.

#3. Sell long-term project bonds to the FFB (HUD and Treasury request).

a. Have Treasury seek the necessary interest differential appropriation.
b. Have HUD seek the necessary interest differential appropriation.

#4. Submit legislation limiting annual contributions to public housing projects financed with taxable LHA obligations (OMB recommendation).

Analysis

Impact on Treasury Revenues/Outlays Budget Authority- ($ in millions)	1976 TR	1976 BA/O	1977 TR	1977 BA/O	1978 TR	1978 BA/O	1979 TR	1979 BA/O	1980 TR	1980 BA/O	1981 TR	1981 BA/O	1982 TR	1982 BA/O
Current policy:														
Alt. #1--Value of tax benefit 1/	-139	NA	-178	NA	-219	NA	-245	NA	-270	NA	-270	NA	-270	NA
Change from current policy:														
Alt. #2--Value of tax benefit and increase in project financing costs 2/ 3/	---	---	-31	+36	-63	+107	-80	+165	-100	+205	-110	+240	-120	+265
Alt. #3:														
. Impact on Federal revenues 4/	---	NA	+?	NA	+?	NA	+?	NA	+?	NA	+?	NA	+?	NA
. Interest differential appropriation 5/	NA	---	NA	+59	NA	+118	NA	+150	NA	+185	NA	+205	NA	+225
. Increase in Treasury borrowing costs	NA	---	NA	+72	NA	+72	NA	+39	NA	+42	NA	+24	NA	+24
. Capital purchase of project bond 6/	NA	---	NA	(+2630)	NA	(+2630)	NA	+1470	NA	+1570	NA	+910	NA	+900
Alt. #4--Impact on Federal revenues and increase in project financing costs 7/	---	---	+?	+69	+?	+207	+?	+315	+?	+395	+?	+460	+?	+505

1/ Value of tax benefit based on an estimated 5.5 percent yield for Treasury bills of comparable maturity to project notes and a 48 percent marginal tax rate for project note holders.

2/ Value of tax benefit based on estimated 8.0 percent yield for Treasury bonds of comparable maturity to project bonds and a 48 percent marginal tax rate for bond holders.

3/ Increase in financing costs is based on an estimated 275 basis points spread between short-term and long-term tax-exempt guaranteed obligations.

4/ Treasury revenues would increase, but the amount of the increase and whether it would cover the interest differential and increased borrowing costs are indeterminate.

5/ Interest differential appropriation is based on estimated 225 basis points spread between high quality tax-exempt bonds and Treasury bonds.

6/ The FFB is shown on-budget starting in 1979 consistent with Director's Review decisions on the 1979 legislative package for Treasury.

7/ Increase in financing costs is based on an estimated 525 basis points spread between guaranteed, short-term tax-exempt notes and guaranteed, long-term taxable bonds and represents the additional annual contributions necessary to support the same number of units that can be supported with the available contract authority under current policy.

Alternative #1.--Continue to roll-over project notes. Given appropriation action to date, the maximum potential sale of public housing bonds--either on the private market or to the FFB--is $10.1 billion. HUD estimates that the current volume of outstanding short-term notes ($5.3 billion) will grow to $8.3 billion by the end of 1978 if no long-term financing is found. The table above assumes the $10.1 billion maximum potential volume outstanding will be reached in 1980. HUD does not feel it can efficiently continue to roll-over such a large volume of short-term notes.

Pros

- At current market conditions, the roll-over of public housing notes provides a lower financing cost and, hence, a smaller foregone revenue than longer term financing.

- Current policy avoids possible disruption of long-term tax-exempt market from issuance of project bonds.

Cons

- Current policy would increasingly tax HUD administratively.

- Short-term notes do not match the economic life of the public housing being financed.

- The volatility of short-term rates exposes HUD and the LHAs to periodic interest rate risk.

- Current policy includes an indirect tax subsidy.

Alternative #2.--Replace project notes with project bonds. The alternative of selling 40-year bonds is opposed vigorously by Treasury. Because the bonds would be effectively guaranteed by HUD, Treasury staff feel they would be superior to other tax-exempt bonds and would force unguaranteed borrowers to pay prohibitively higher interest or to leave the market. Implicitly, Treasury's position assumes that the demand for long-term, tax-exempt investments is relatively inelastic. Significantly, the majority of long-term tax-exempt borrowing is for housing purposes (e.g., State

Housing Finance Agencies). The higher costs and/or reduced supply of credit could reduce the ability of these borrowers to complement Federal housing subsidy programs and might lead to a larger demand for direct Federal assistance. Additionally, Treasury fears the impact of adding the $8-10 billion of bonds to a market only $25-30 billion in breadth. While not totally disagreeing with Treasury analysis, HUD and OMB staff do not think project bonds would be as disruptive as Treasury staff do, especially if the issuance of bonds is staggered.

Pros

- The sale of long-term bonds would:

  . Relieve HUD administratively.
  . Tie the financing more closely to the useful economic life of public housing projects.
  . Eliminate the exposure to more volatile short-term rates.

- To the extent contract authority remained unchanged, the higher financing cost would reduce the number of public housing units that could be assisted with current appropriations.

Cons

- If not carefully controlled, the issuance of public housing bonds might make credit more costly and/or less available for State and local programs which complement HUD's mission.

- At current market rates, the indirect tax benefit subsidizing public housing construction would increase.

- This alternative would continue the use of an indirect tax subsidy.

- The increased financing cost would create incentives to appropriate new contract authority to maintain the level of public housing activity originally envisioned for 1977.

Alternative #3--Sell project bonds to the FFB. HUD and Treasury propose to permanently finance public housing through the sale of project bonds to the FFB. The table above assumes that the FFB would provide permanent financing for the current $5.3 billion volume of outstanding notes in 1977 and 1978. Because of an estimated 2-year lag between HUD approval to begin development and acquisition and the point of permanent financing, the FFB would not begin to purchase bonds resulting from the 1977 appropriation until 1979. The table above estimates the FFB would purchase the maximum potential amount of bonds, $10.1 billion. The purchase would not be complete until 1982 under these assumptions. The HUD/Treasury proposal does not address the question of how much of the potential volume of bonds should be sold to the FFB.

If the bonds were sold to FFB, the differential between the interest realized by the FFB and that paid on Treasury borrowing financing the purchases would have to be covered with a current appropriation. The FFB would be protected from the loss of principal by the annual contribution contract between HUD and the LHAs, much as private holders of project notes and bonds are currently protected. The HUD/Treasury proposal does not consider which agency should seek the interest differential appropriation. The omission was deliberate because the agencies could not reach agreement. Although there would be no difference in budget or fiscal policy impact, the choice of agency to finance this differential would have political impact.

Selling project bonds to the FFB would make all the Federal subsidies for public housing explicit. The indirect interest subsidy currently flowing from the tax-exempt status of LHA debt would become explicit in the form of the interest differential appropriation.

Also, as a budget principle, Treasury and OMB/BRD have opposed Federal guarantees of tax-exempt debt. Selling project bonds to the FFB would eliminate a substantial portion of federally guaranteed, tax-exempt debt and convert it to direct Federal loans. The FFB purchases of project bonds would constitute an off-budget, Federal outlay. However, the 1979 legislative program approved at the Director's Review for Treasury included a proposal to place the FFB on-budget in 1979. Accordingly, the table above shows the FFB purchases on budget starting in 1979. Of course, as the bonds held by the FFB are retired, the FFB would register offsetting receipts. Purchases of project bonds by the FFB would be the budgetary equivalent of compressing into a 4 or 5 year period the outlays that would otherwise occur over 40 years as HUD liquidated annual contributions contracts.

Replacing tax-exempt credit with taxable credit would increase Treasury revenues; however, there is a question of whether the revenues would increase enough to offset the interest differential subsidy. Treasury staff maintain that the replacement of tax-exempt credit with taxable credit will always result in a net reduction of the Federal deficit. OMB and HUD staff maintain that the net impact on the deficit depends on investor response to the reduction in the supply of tax-exempt credit and the increase in taxable credit (the additional Treasury borrowing to finance FFB purchases). Only if enough investors leave the tax-exempt market and reduce demand enough to stabilize yields at the same level as that prior to sales and only if the average marginal tax bracket of the investors shifting to the taxable market corresponds to the average of all investors prior to the sales would the increased Treasury revenues just offset the interest differential appropriation. There would be variations from year to year. In some years, the additional Treasury revenues would be greater than the interest differential appropriation and the Federal deficit would be less than it would otherwise be; in other years, the revenues would be less and the deficit larger.

Pros

- Sales of project bonds to the FFB would advance the following budget principles:

    - The Federal Government should not guarantee tax-exempt debt.

    - Subsidies should be explicit and direct rather than implict and indirect.

- HUD would be relieved from continuously turning over a high volume of short-term notes.

- LHAs would get permanent financing without resorting to the long-term tax-exempt credit market. This would:

    - Provide financing consistent with the economic life of public housing.
    - Avoid disrupting the State housing programs which complement HUD programs.

Cons

- On budget FFB outlays starting in 1979 would make the goal of a balanced budget in 1979 more difficult.

- The interest differential appropriation would increase the budget base for the agency seeking the appropriation. Neither HUD nor Treasury is happy with this prospect. Constituents of the respective agencies would object to this increase that provides no new additional benefits to them.

- Commercial bankers might give organized opposition. In addition to the tax-exempt income source they would lose, they would face a reduced supply of investments which many local jurisdictions require as a precondition for the deposit of local government funds.

Alternative #4 (OMB recommendation). Limit annual contributions to LHAs that employ only taxable obligations to finance public housing. This alternative would require legislation, and would increase the interest cost of financing each public housing unit. The table above estimates the additional interest cost to finance the same number of units currently contemplated. Of course, contract authority and annual payments could be held level by financing fewer units. The estimate above also assumes the full potential requirement for permanent financing would be done with taxable guaranteed bonds. The increased contract authority required per unit is also, in effect, a conversion of the indirect tax subsidy to a direct annual grant. While the reduction of tax-exempt credit and the increase of taxable credit would increase Treasury revenues, it is not clear what the net impact on the deficit would be for the same reasons as outlined in the discussion of Alternative #3 above.

Pros

- Limiting annual payments to projects with taxable financing only would provide financing more consistent with economic life of public housing and eliminate HUD's problems in continuously rolling over short-term debt.

- This form of financing would not have the budget outlays registered in a short span of time as under Alternative #3, avoiding the adverse impact on 1979 budget goals.

- Taxable financing would make the subsidy resulting from tax-exempt status explicit and direct in the form of higher annual payments per project.

- LHAs would be using the broad, taxable credit markets and would avoid the potential problems of using the long-term tax-exempt market.

- If contract authority were not increased, a political windfall would be realized in the smaller number of units which would be built with the 1977 contract authority which was enacted over Administration opposition.

Cons

- The required legislation would be difficult to obtain. The public housing constituency would object to the higher costs per unit.

- If the necessary legislative changes occurred, Congress might appropriate additional contract authority to maintain program levels.

HUD Request: Alternative #3. HUD and Treasury feel that it is financially and administratively undesirable to continue to roll-over short-term notes. They propose to resturucture LHA debt by selling bonds to the FFB.

OMB Recommendation: Alternative #4. Submitting legislation limiting annual payments to LHAs using only taxable financing would advance the budget principles that the Federal Government should not guarantee tax-exempt debt and that explicit, direct subsidies are preferable to indirect tax subsidies. It would also avoid an adverse impact on 1979 budget goals. Further, the increased financing costs per project should be absorbed within existing contract authority by reducing the number and/or size of projects. This would avoid the extra outlays shown for Alternative #4 on the table above.

#4. FHA

Issue Paper
Department of Housing and Urban Development
1978 Budget
Issue #4: Federal Housing Administration

SUBISSUE A: Future Role of FHA

Background

Following the Spring Review of FHA's role in the mortgage market, HUD and OMB staff were able to reduce the number of major issues to one or two. HUD had almost finalized its study when the President announced three initiatives to accelerate homeownership:

- Lower FHA downpayments (legislation required).
- Increase FHA mortgage limits (legislation required).
- Accelerate the experimental homeownership insurance program.

Although these initiatives have not necessitated any substantive changes in the recommendations, the Secretary has asked to have the study rewritten. It should be transmitted officially to OMB later this month.

The recommendations are discussed below. The budget impact of all the FHA study recommendations are presented at the end of this paper. Although the Secretary has apparently endorsed the major recommendations of the study, the impact of these recommendations has not been reflected in her 1978 budget request.

1. Should FHA continue to provide default insurance on single-family mortgages?

Comment: Basic agreement reached: FHA should provide single-family insurance in a manner that is complementary to the private market, taking whatever actions are necessary to make FHA less competitive with private mortgage insurers (PMI's).

2. Should FHA continue to provide default insurance on multifamily mortgages?

Comment: Basic agreement reached: FHA should continue to provide multifamily insurance, but changes should be made to encourage PMI multifamily insurance as discussed below.

3. Should mortgage insurance premiums be established on an actuarially sound basis, and if so, how?

Comment: basic agreement reached: Actuarially sound premiums should be charged under each individual program, to the extent current law permits. Premiums should vary with the loan-to-value ratio.

4. Should the Federal Government directly subsidize part of an actuarially sound premium for low- and moderate-income families in order to encourage homeownership?

Comment: Basic agreement reached: No program of mortgage insurance for low-income families (other than section 235) should be provided, and the low- and moderate-income single-family program (section 221(d)(2)) should be terminated.

5. Should the Federal Government directly subsidize part of an actuarially sound premium in older, declining areas?

Comment: HUD and OMB staff agree that the section 223(e) program for older, declining areas should be terminated. However, HUD will propose to directly subsidize actuarially sound premiums in neighborhood preservation areas. HUD is developing criteria for administering such a program, and a decision should be postponed until these criteria can be reviewed.

6. Should statutory limitations be changed?

Comment: Basic agreement reached: Current statutory limitations include FHA interest rate ceilings, per-unit mortgage limits, and downpayment requirements. The Administration has already proposed to let the private market, rather than HUD, set each mortgage's interest rate. Removing mortgage and downpayment requirements would give the Administration greater flexibility in meeting the objective of complementarity.

7. What should be the Administration's policy on loan management and property disposition of FHA's housing inventory?

Comment: Currently, HUD's paper does not address loan management and property disposition. However, HUD staff have agreed to develop a study plan to comprehensively address these issues. Budget decisions are needed on several inventory issues that are addressed separately.

Budgetary Effects of FHA Study Recommendations

Budget Authority/Outlays ($ in millions)	1976 BA	1976 O	1977 BA	1977 O	1978 BA	1978 O	1979 BA	1979 O	1980 BA	1980 O	1981 BA	1981 O	1982 BA	1982 O
Current policy - status quo	1231	1191	1404	1315	1452	1362	1212	1212	1247	1247	1281	1281	1315	1315
Change from current policy:														
HUD informal request and OMB recom.	---	---	---	---	-20	-20	-37	-37	-62	-62	-79	-79	-82	-82

These outlay estimates only cover the direct impact of (1) elimination of rebates, (2) increased premium income, and (3) reduced actuarially unsound insurance. No estimates are made for less-than-major recommendations.

No disagreement exists on programmatic recommendations between HUD and OMB staff. A number of disagreements have been previously surfaced, then studied by both staffs and resolved by an agreement or deferral of the issue, pending better analysis or program definition. We expect that the issue of subsidizing actuarially sound premiums in neighborhood preservation areas will be raised by a HUD proposal before the 1978 budget is finalized.

Next Steps

OMB recommends passing back the draft FHA study recommendations to HUD as Presidential decisions. HUD should be directed to develop:

- Legislative proposals and supporting explanations to implement the recommendations. These materials should be provided by January 1, 1977, so that they may be referenced in the State of the Union message.

- Estimates of the 1978-1982 budget and employment impact of each recommendation.

SUBISSUE B: Single-Family Property Disposition

Statement of Issue

What should be the property disposition strategy and sales levels for single-family properties in 1977 and 1978?

Background

HUD acquires foreclosed single-family properties as mortgage insurance claims are paid. The high level of insurance activity, particularly in the risky programs, coupled with unsound underwriting practices, led to large increases in property acquisitions between 1970 and 1975, as shown below.

	1972	1973	1974	1975	1976	TQ
Acquisitions........	52	61	61	53	37	8
Sales................	32	39	51	66	56	19
Inventory EOY.......	53	75	85	72	53	43

- Almost one-half of the current inventory has been owned by HUD for over a year. Only one-third has been in HUD's inventory for less than 6 months.

- Almost 60 percent of the units are in five major cities; over 25 percent of the units are in "inner city core areas."

HUD has two primary property disposition approaches:

- Repair, sell, and insure where the property is brought up to FHA's minimum property standards and then sold with FHA insurance.

- As-is sales without insurance where the highest cash offer is accepted for the unimproved property.

Following a major property disposition study and a limited survey which indicated that the costs of repair usually exceeded any increase in sales price, the Department decided to increase the emphasis on "as-is"/all cash sales, and the 1976 and 1977 Budgets reflected it. Most of the increase in recent sales has come from as-is sales, which climbed from 35 percent of total sales in 1974 to 48 percent in 1975, and 54 percent in 1976. Repair and rehabilitation still accounted for almost half of the sales in 1975. Carrying costs per day for each unit in the inventory average around $7.

Despite recent increases in the as-is share of sales, HUD now plans to shift the emphasis back to the repair and sell approach. This approach is seen as more consistent with the Secretary's emphasis on increased use and improvement of the existing housing stock. HUD's lower sales targets for 1977 and 1978 reflect both this switch in strategy and the anticipated decline in unit acquisitions, but HUD does not disaggregate these influences.

Alternatives

#1. Accept HUD's reduced emphasis on "as-is" sales and estimates of sales below the 1977 budgeted level in 1977 and 1978 (HUD request).

#2. Encourage an increased emphasis on as-is sales by reducing holding times and setting inventory targets of 29,000 and 20,000 units in 1977 and 1978, (OMB recommendation).

#3. Accept HUD's estimate of sales, but establish a ceiling in the 1978 apportionment for the FHA Fund that limits the amount available for repair and sell.

Analysis

Budget Authority/Outlays	1976		1977		1978		1979		1980		1981		1982	
($ in millions)	BA	O	BA	O	BA	O	BA	O	BA	O	BA	O	BA	O
Current policy Alt. #2	1226	1191	1372	1283	1416	1326	1194	1194	1229	1229	1263	1263	1295	1295
Change from current policy:														
Alt. #1 (HUD request)	0	0	+32	+32	+36	+36	+18	+18	+18	+18	+18	+18	+18	+18
Alt. #2 (OMB recom.)	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Alt. #3	0	0	0	0	0	0	0	0	0	0	0	0	0	0

	HUD Request 1977	HUD Request 1978	OMB Recommendation 1977	OMB Recommendation 1978
	(Thousands of Housing Units)			
Acquisitions	33	29	33	29
Sales.......	43	35	47	38
Inventory...	33	27	29	20

HUD and OMB agree that "as-is" sales are the fastest way to dispose of HUD's acquired property and usually provide the highest return to the FHA Fund for most acquired properties by reducing holding costs, Federal staffing, and vandalism associated with a large number of vacant units. HUD believes the repair and rehabilitate approach helps attain some additional social objectives such as housing supply preservation, minority contracting, neighborhood stabilization, and low-income subsidies.

Substituting repair and rehabilitation sales for as-is will (1) improve public relations with city officials; and (2) permit some attainment of social objectives, but will also provide a slower disposition of the inventory. Specific estimates of the net loss per repair sale and the value associated with these public relations and social objectives are not available. Negative relations with city officials have occurred to the extent that some cities (Detroit and Philadelphia) have passed laws to prohibit massive as-is sales.

The reduced emphasis on as-is sales (Alternative #1) would reduce confrontations with city officials and neighborhood groups who prefer HUD's rehabilitation and insurance of the properties. Property disposition would be better able to serve the nonfinancial housing supply objectives. Relations with local governments would be improved.

HUD's request would slow the decline in inventory reduction. Most of the 27,000 remaining units would continue to be held in inventory over a year and would be located in central city core areas.

Reducing holding times and setting a lower inventory target (Alternative #2) would encourage as-is sales, but still allow HUD to use all the available authorities to meet the President's budget goals. The need for a lower-than-requested target could cause HUD to emphasize some of the social objectives and take a little more heat in the public relations area. This approach gives the Department the Administration's desired target without specifying how to get there.

OMB's recommendation would continue the improvement in inventory reductions down to 20,000 units in 1978. HUD would have to sell cheaply, give to cities or raze a number of older, core area properties rather than continue hanging on to them. Carrying costs and local taxes paid would be reduced.

HUD has had difficulty meeting specific sales targets in the past, in part because acquisitions have fallen short of budget estimates. Setting an inventory target avoids this problem, but still enforces some budget discipline.

No accounting basis currently exists to establish a ceiling in the 1978 FHA apportionment that would limit the amount available for repair and sell (Alternative #3). Repair and other costs are netted from sales revenue in field reports and the detailed accounting system includes repairs with other nondisposition program costs. An apportionment limit could be developed for repairs, but this would implicitly and rigidly prejudge field decisions on the choice of disposition approaches: after the apportionment limit had been reached, OMB would be prejudging that all other sales should be as-is. Unlike the inventory target system (Alternative #2), an apportionment limit would not give the Secretary the discretion in determining how to get to the desired goal and also would not flexibly adjust to acquisition changes.

HUD Request: Alternative #1. The reduced emphasis on as-is sales allows other objectives and approaches to be fully considered. Reductions in inventory targets would make it more difficult to fully consider social objectives and would lead to confrontations with locally elected officials.

OMB Recommendation: Alternative #2. OMB recommends reducing the end-of-year inventory targets and reducing average holding times to encourage as-is sales. If this inventory target system does not work, we will further consider an apportionment limit (Alternative #3).

SUBISSUE C: Residual Multifamily Inventory

Statement of Issue

What actions should be taken to reduce the growing multifamily inventory?

Background

HUD's multifamily inventory has been growing at a rapid rate in the 1970s as assigned mortgages have accumulated:

	1972	1973	1974	1975	1976	TQ
Assigned mortgages	16,032	30,235	34,804	58,866	65,098	19,968
Acquired property	4,418	9,161	14,000	17,570	10,271	8,692
Property sales	2,803	8,338	9,681	10,267	14,672	5,615
Inventory, end-of-period	91,916	113,030	140,798	194,716	246,674	261,229

If the mortgages that have been assigned to HUD were making their full monthly mortgage payments, HUD would be receiving $253 million annually. Actual mortgage payments are only $127 million, or half of the amount due.

Alternatives

#1. Current policy of holding assigned mortgages indefinitely.

#2. Increase foreclosures and sales estimates (HUD request).

#3. Increase foreclosures and sales estimates, but also set an inventory target in the PMI and HUD's GMS systems (OMB recommendation).

Analysis

Budget Authority/Outlays ($ in millions)	1976 BA	1976 O	1977 BA	1977 O	1978 BA	1978 O	1979 BA	1979 O	1980 BA	1980 O	1981 BA	1981 O	1982 BA	1982 O
Current policy Alt. #1	1231	1191	924	835	1352	1262	1212	1212	1247	1247	1281	1281	1315	1315
Change from current policy:														
Alt. #2 (HUD request)	---	---	-480	-480	-100	-100	---	---	---	---	---	---	---	---
Alt. #3 (OMB rec.)*	---	---	-563	-563	-265	-265	-165	-165	-165	-165	-165	-165	-165	-165

* Includes $350 million of 1977 mortgage sales that is an open issue which depends on the budget totals. Also includes $165 million estimate of savings from sales after deeds-in-lieu are accepted.

	1976 Actual	TQ Estimate	1977 HUD	1977 OMB	1978 HUD	1978 OMB
Assigned mortgages	65,098	19,968	55,000	55,000	68,000	68,000
Acquired property	10,271	8,692	35,786	35,786	37,664	37,664
Mortgage sales	---	---	70,000	70,000*	---	---
Foreclosures	8,739	7,801	32,167	32,167	33,400	33,400
Deeds-in-lieu	---	---	---	25,000	---	50,000
Property sales	14,672	6,304	54,411	54,411	43,354	43,354
Inventory, end-of-period	246,674	261,229	195,437	170,437	224,347	149,347

* Same as footnote above.

The following are the legal alternatives to reduce HUD's multifamily inventory:

- Avoid assignments and acquisitions (principally through the use of section 8 subsidies--see issue #1B).

- Do not provide for assignment of mortgages in new insurance contracts.

- Sell assigned mortgages.

- Foreclose and sell property.

- Accept deeds-in-lieu and sell the property.

- Sell acquired property from the inventory.

Mortgage Sales

The Secretary and her staff realize the seriousness of HUD's growing multifamily inventory problem. She has proposed to reduce the pool of assigned mortgages by selling those that are current in their mortgage payments. Her proposal assumes that most of the mortgages would be sold without insurance, but indicates that 58 of the 565 projects are subsidized and would need either insurance or section 8 subsidies to be saleable. The Secretary's proposed sale of assigned mortgages with $500 million in unpaid principal is estimated to yield $350 million in receipts in 1977. It is estimated that, on a discounted present value basis, a private market sale of these mortgages would yield only 68 percent of the current outstanding balance, as compared to a 79 percent return if the mortgages are held. This would mean a $55 million loss to the fund, not counting future insurance losses we can expect on those mortgages sold with insurance. On the other hand, breaking HUD's link to over 500 multifamily projects would insulate the Government against further losses.

Property Sales

HUD is predicting an almost four-fold increase in sales between 1976 and 1977. A three-fold increase over 1976 sales is predicted for 1978. Although it will be very difficult to reach these targets, we believe they should be approved. To reach them, it will be necessary to foreclose hopeless projects and sell them at market prices. The Department agrees that foreclose-and-sell is considerably more cost-effective, even though it is politically more painful.

Including an inventory target system in the Presidential Management Initiatives and HUD Goals Management System would have a number of benefits for multifamily inventory management:

- The system would be flexible enough to account for variations in the volatile estimates of assignments.

- Sales and other disposition techniques would be adjusted to changing assignments and acquisitions.

- Strong incentives would be built into the system to avoid assignments.

- The Secretary would have to account to the President for any increase in outlays.

Deed-in Lieu

Under current law, HUD is allowed to accept a deed-in-lieu rather than foreclosing on a mortgage to obtain title. HUD uses this authority gingerly because it is fraught with dangerous possibilities:

- A complete audit of financial information about the project is required before a deed-in-lieu is accepted since HUD must then accept all liens and cannot seek reimbursement due to fraudulent practices. The audit and other checking takes so much processing that no time is saved compared to a foreclosure process (both now take about 2 years).

- A policy of lenient acceptance of deeds-in-lieu would allow mortgagors to completely "rip-off" their project before turning it over to HUD.

- HUD could also be obligated for liens against the project that are not uncovered at the time a deed-in-lieu is accepted.

However, given the intractable state of the assigned project inventory (which HUD estimates to be over 200,000 units at the end of 1978), a deed-in-lieu approach could be developed as a "friendly foreclosure" for nonprofit sponsor projects. HUD previously has been unable to foreclose on churches, labor unions, etc., and nonprofits are poor financial managers with high risk and loss rates. Therefore, the status quo policy of holding assigned mortgages indefinitely is not desirable. Nonprofit sponsors are also unwilling to put more resources in a failing project, so there is little to gain from keeping them as owners. Given the political difficulty of suing the church, a deed-in-lieu would not forego much in the way of damages or other returns. However, it would enable HUD to acquire property that could be resold. To protect the existing tenants, HUD could use existing section 8 authority or impose a 5-year limit on rent increases.

HUD Request: Alternative #2. HUD would sell assigned mortgages in 1977 and acquired properties as shown in the table above

OMB Recommendation: Alternative #3. While we would recommend against HUD's proposed sale of assigned mortgages on financial grounds, we realize that asset sales may be necessary to obtain the desired budget totals in 1977, 1978, or 1979. An inventory target should be included in the Department's Goals Management System, in order to add the elements of enforceability and budget discipline to the Secretary's "estimates." We recommend inventory targets of 170,000 units at the end of 1977 and 112,000 units at the end of 1978. These targets reflect the recommended section 8 set-aside for FHA projects and the deed-in-lieu units. The mortgage sales issue would be left open, but the unit reduction would be temporarily included in the inventory targets.

So far, HUD staff have not come up with any feasible way to reduce the growing assigned project inventory. We recommend passing back to HUD a proposed deed-in-lieu program for 25,000 units in 1977 and 50,000 units in 1978 in order to (1) get a positive reaction to the possibilities of a deed-in-lieu program, or (2) force some more attractive alternatives for reducing the assigned inventory out of the Department. Since we can offer no assurance that a feasible approach to reducing the assigned multifamily inventory can be devised, we have not included any savings in our internal OMB-recommended totals. Finally, we recommend that all future mortgage insurance contracts give HUD the option of accepting mortgage assignments, instead of leaving it up to mortgagees.

#5. COUNSELING

Issue Paper
Department of Housing and Urban Development
1978 Budget
Issue #5: Homeownership Counseling

Statement of Issue

Should HUD initiate a homeownership counseling program in 1977 and continue it in 1978?

Background

In the 1977 Budget HUD requested no funds for counseling. Congress, however, appropriated $3 million for this activity. HUD has supported and encouraged homeownership counseling in a variety of ways but currently does not have a categorical counseling program.

. Counseling is an eligible activity under the CDBG program when provided in connection with local HAPs.

. Homeownership information, advice, and assistance is available from HUD staff to purchasers of HUD owned property in 1-hour counseling sessions.

. The 1974 Housing and Community Development Act requires HUD to provide counseling to section 235 recipients. It also contains an open-ended appropriation authorization for counseling assistance.

Alternatives

#1. Propose rescission of funds provided for counseling in 1977, and request no additional funds in 1978 (OMB recommendation).

#2. Allow HUD to use appropriated funds in 1977 for one time grants, but seek no additional funds in 1978.

#3. Implement the program in 1977, and continue it in 1978 at a $6 million funding level (HUD request).

Analysis

Budget Authority/Outlays ($ in millions)	1976		1977		1978		1979		1980		1981		1982	
	BA	O	BA	O	BA	O	BA	O	BA	O	BA	O	BA	O
Current policy (Alt. #1 OMB recommendation)	1	1	--	--	--	--	--	--	--	--	--	--	--	--
Change from current policy:														
Alt. #2	--	--	+3	+3	--	--	--	--	--	--	--	--	--	--
Alt. #3	--	--	+3	+3	+6	+6	+6	+6	+6	+6	+6	+6	+6	+6

HUD and OMB agree that:

. Counseling cannot harm, and may help, delinquent homebuyers.

. HUD must do something for section 235 homebuyers in order to satisfy the statutory mandate, but this need not involve face-to-face counseling. HUD could meet the 1974 Act's requirements by distributing counseling brochures to section 235 recipients.

There are several other sources that counseling and funds for such activities can come from:

. They can be provided under community development block grants.

. HEW funds counseling programs directed at low- and moderate-income groups.

. Localities should be encouraged to treat subsidized housing and low-income groups as part of their overall population and deal with their needs as such.

HUD Request: Alternative #3. The Secretary believes that counseling is cost-effective and wants to fund the program at a $6 million level in 1978.

OMB Recommendation: Alternative #1. Propose rescission of funds provided for counseling in 1977, and request no additional funds in 1978.

#6. OTHER HOUSING
ISSUES

Issue Paper
Department of Housing and Urban Development
1978 Budget
Issue #6: Miscellaneous Housing Issues

SUBISSUE A: Urban Homesteading

Statement of Issue

What level of activity should be approved under HUD's Urban Homesteading Program?

Analysis

Budget Authority/Outlays ($ in millions)	1976 BA	1976 O	1977 BA	1977 O	1978 BA	1978 O	1979 BA	1979 O	1980 BA	1980 O	1981 BA	1981 O	1982 BA	1982 O
Urban Homesteading:														
HUD Request	6	6	15	15	15	15	0	0	0	0	0	0	0	0
OMB Recommendation	6	6	15	15	15	15	0	0	0	0	0	0	0	0

The status of HUD's Urban Homesteading Program is shown below:

	As of October 22, 1976
Program announced in October 1975	
Agreements with 23 cities signed in December 1975	
Current progress:	
Units conveyed to cities	762
Homesteaders selected	663
Conditional conveyances	476
Financing arranged*	400
Rehabilitation begun	411
Families occupying	271

* Mostly private financing: A few section 312 rehabilitation loans and very little FHA insurance.

A well designed, major evaluation has begun of the Urban Homesteading Program which was funded with a $5 million supplemental in 1976. In the last televised debate, the President indicated that HUD's Urban Homesteading Program was being expanded. HUD has announced an additional release of $1.25 million provided in the 1976 Authorization Act. The Act also authorized $5 million in 1977 and 1978.

HUD Request: An additional $15 million for both 1977 and 1978 (authorizing legislation required). HUD estimates that a $15 million level will help dispose of 3,000 additional units per year. A legislative proposal is pending in HUD for multifamily urban homesteading authority, but no program specifications have been developed.

OMB Recommendation: The demonstration seems to be going as well as could be expected for a new initiative. An in-depth evaluation of the program is underway. We recommend funding the program at the $15 million level requested. The inventory targets for property disposition will be adjusted to reflect this annual 3,000-unit reduction.

SUBISSUE B: Indian Housing

Statement of Issue

Should the Indian Housing Program be continued in 1978, and, if so, at what level?

Background

The Indian population is one of the most ill-housed minorities in the United States today. A FY 1976 housing survey conducted by the Bureau of Indian Affairs shows a need of 58,000 new units and 25,900 units suitable for renovation. Although the Indian Housing Program has been authorized at a 6,000 unit level for FY 1975 and FY 1976, new starts in FY 1976 and the transition quarter were only 1,200. At the end of FY 1976/TQ 9,465 units approved under the Indian Housing Program had not been started. This amounts to 1.7 years worth of approvals, or over 9-years-worth of starts (FY 1976 rate). The Indian Housing Program has suffered from internal management problems and poor coordination with other agencies delivering services to Indians, especially BIA and IHS.

Alternatives

#1. Continue 6,000-unit program level in 1978 (HUD request).

#2. Establish 1,000-unit level for 1978 (OMB recommendation).

#3. Provide no new budget authority in 1978, but allow program to continue by using carryover authority.

Analysis

Budget Authority/Outlays ($ in millions)	1976		1977		1978		1979		1980		1981		1982	
	BA	O	BA	O	BA	O	BA	O	BA	O	BA	O	BA	O
Current policy (Alt. #1)	864	13	960	16	1056	26	1161	29	1277	32	1405	26	2061	51
Change from current policy:														
Alt. #2 (OMB recom.)	---	---	---	---	-880	-4	-967	-24	-1064	-27	1171	-29	1803	-45
Alt. #3	---	---	---	---	-1056	-4	-1161	-10	-1277	-32	1405	-26	2061	-51

HUD has proposed an Indian Housing Program level of 6,000 units in 1978 and housing starts are expected to increase dramatically as the table below indicates.

Reservations			Starts			Completions		
1976/TQ	1977	1978	1976/TQ	1977	1978	1976/TQ	1977	1978
8,465	8,000	6,000	1,200	5,460	9,000	3,500	4,000	6,000

While HUD has worked to overcome some of the management problems surrounding this program, OMB believes some problems still remain. The principle ones are:

. Lack of training. A variety of technical assistance programs needs to be developed in order to assure that the IHAs get proper training to carry out procedures expediently.

. Lack of coordination among the agencies dealing with Indian housing.

Even if these management problems were eliminated, the increase in new starts would be a large order.

HUD has been unable to provide good reasons for believing the 9,000 starts projected in 1978 can be reached. A high level of starts can still be maintained in 1978 with no new budget authorizations because of carryover from previous years.

Pro: This would lower budget authority without affecting the program level as there is a large backlog of housing.

Con: Not authorizing any additional units for 1978 would give the appearance of terminating the Indian Housing Program, which would result in a political "black eye."

Allowing authorization of 1,000 units would (a) cut budget authority by five-sixths, (b) avoid the negative impression of terminating the program, and (c) stimulate HUD to get the reservations out of the pipeline.

HUD Request: Alternative #1.

OMB Recommendation: Alternative #2.

SUBISSUE C: College Housing

Statement of Issue

What course of action is mostly likely to achieve termination of the college housing program?

Background

Although the Administration proposed terminating this program in the 1977 Budget, Congress failed to do so, and the appropriations committee report directed HUD to continue it for another year.

There is no disagreement over the program's merit: HUD, OMB, and many members of Congress agree that it should be terminated. However, individual colleges have kept it alive by bringing pressure to bear on key congressmen.

Analysis

Budget Authority/Outlays	1976		1977		1978		1979		1980		1981		1982	
($ in millions)	Obl.	O	Obl.	O	Obl.	O	Obl.	O	Obl.	O	Obl.	O	Obl.	O
Current Policy..........	-9	-49	---	-72	---	-97	---	-101	---	-97	---	-108	---	-119
Change from current policy:														
HUD request and OMB recommendation.......	---	---	---	+21	---	+86	---	+48	---	---	---	-6	---	-6

HUD Request and OMB Recommendation: Release all unobligated funds in FY 1977 ($155 million) and once again include language in the budget that would transfer the College Housing Fund to the revolving fund in FY 1978. Although this will increase outlays significantly during 1978 and 1979, HUD and OMB agree that a more direct assault on the program (such as proposing a rescission) would make it more difficult to get rid of the program.

#7. CDBG

Issue Paper
Department of Housing and Urban Development
1978 Budget
Issue #7: Community Development Block Grants

Background

Section 106 of the Housing and Community Development Act of 1974 requires the Secretary of HUD to report to Congress no later than March 31, 1977, her recommendations for modifying the block grant allocation formula based on her determination of community development needs, objectives, and capacities, measured to the maximum extent feasible by objective standards. The conference report on the Act specifies that the formula and hold-harmless provisions for distributing funds should be subjected to systematic study and full review before additional funds are authorized. The Secretary's recommendations are also to include an in-depth exploration of the feasibility of making regional adjustments in the measure of poverty.

An appropriation authorization for 1978 and 1979 will also be required for the Community Development Block Grant (CDBG) Program.

SUBISSUE A: Funding Level

Statement of Issue

What should be the level of funding for the CDBG program in 1978 and 1979?

Alternatives

#1. Provide a program level constant with 1977--$3,148 million (OMB recommendation).

#2. Provide a $3,344 million level--the 1977 level of $3,148, plus $196 million for inflation--in 1978 and 1979 (HUD request).

#3. Take part of the savings from the phasedown of hold-harmless and instead of putting them into the program for use by other recipients, decrease the program level to $2,900 million with a resulting decrease in outlays.

Analysis

Budget Authority/Outlays*	1976		1977		1978		1979		1980		1981		1982	
($ in millions)	BA	O	BA	O	BA	O	BA	O	BA	O	BA	O	BA	O
Current policy (Alt. #1 OMB recommendation)	2752	308	3148	2382	3148	3001	3148	3077	3148	3148	3148	3148	3148	3148
Change from current policy:														
Alt. #2 (HUD request)			---	---	+196	+12	+196	+100	+196	+174	+196	+196	+196	+196
Alt. #3			---	---	-248	-14	-248	-127	-248	-221	-248	-246	-248	-248

* Excludes the Urgent Needs Fund and the funding for urban parks proposed in the Bicentennial Land Heritage Act.

Alternative #1

Pro: Provides a funding level constant with 1977, so that the President can still lay claim to being committed to the program but, while trying to balance the budget, cannot afford more.

Those recipients who expected to receive increased funding with the phase-down of hold-harmless will still get that additional amount.

Con: Does not recognize the decrease in purchasing power of the 1977 funding level as a result of inflation.

Alternative #2

Pro: Providing a steady program level that also recognizes the impact of inflation shows good faith on the part of the Administration that (1) this is a program that the mayors can count on and plan their finances against; and (2) the Administration is as committed to CDBG as it is to General Revenue Sharing and is maintaining the buying power of these grants at a steady level.

Con: There is no programmatic justification or indication of need for an additional $196 million. The base is arbitrary to begin with and need not be protected from inflation.

Budgeting for inflation is inconsistent with the budget regulations in A-11.

Alternative #3

Pro: Will provide outlay savings of $127 million in 1979, when the President is attempting to balance the budget.

Con: Decreasing the total funding based on a phasedown of hold-harmless will mean not providing the additional funding for other recipients which they were anticipating.

Throws cause for doubt on the President's statements that the CDBG program and the necessary assistance it provides is of vital importance to him in improving the condition of our cities and neighborhoods.

HUD Request: Alternative #2. Tentatively $3,344 million. Final decisions on changes in the formula may result in a revised number.

OMB Recommendation: Alternative #1. Tentatively $3,148 million until the Department submits a programmatic justification for an increase.

SUBISSUE B: Urgent Needs

Statement of Issue

Should the urgent needs fund be continued in 1978 or thereafter?

Background

Section 103(b) of the 1974 Act authorized appropriations to be made "...for grants... to units of general local government having urgent community development needs which cannot be met through the operation of the /formula/ allocation provisions...." In 1975 and 1976, $50 million was provided each year; in 1977, $100 million was appropriated.

The Department is proposing an extension of a $100 million urgent needs fund at least through 1978. Requirements in 1978 are estimated between $40-$80 million.

Alternatives

#1. Provide a $100 million urgent needs fund in 1978 and 1979 (HUD request).

#2. If there is a need for urgent needs assistance, provide it through the SMSA discretionary balance or the Secretary's discretionary fund (OMB recommendation).

Analysis

Use of the SMSA discretionary balance. Section 106(d) of the 1974 Act provides for use of whatever funds remain after the allocation to entitlement recipients as a discretionary fund for other SMSA local governments and States for use in metropolitan areas other than metropolitan cities and urban counties. Funds are allocated among the SMSAs based on a population/poverty/housing overcrowding formula. In 1978, about $295 million will be available for distribution from the discretionary balance. HUD sees two problems with utilizing these funds as an urgent needs fund: (1) the funds may not go to metropolitan cities, where this need exists; and (2) after the discretionary fund balance is allocated among SMSAs, the amounts for those SMSAs whose metropolitan cities need additional assistance are not large enough to cover the urgent need. However, both of these problems could be eliminated by amending this authority, perhaps to allow the Secretary to tap the discretionary fund to meet urgent needs before allocating the funds to all SMSAs.

Use of the Secretary's discretionary fund. In 1978, the Secretary's discretionary fund will total about $65 million. The Secretary is currently authorized to provide funds "... to States and units of general local government where the Secretary deems it necessary to correct inequities resulting from the allocation provisions of section 106." The conference report on the 1974 Act elaborates on this authority: It "... provides an additional source of grant funds...for communities which may not receive an adequate level of funding as a result of the bill's allocation and distribution provisions. Some communities, for example, will experience substantial cutbacks from their relatively high program levels in the latter years of the FY 1968 - FY 1972 period; others...will have reduced entitlements under the new program primarily as a result of unique local problems...The conferees expect the Secretary to give sympathetic consideration to funding requests from such communities in distributing...discretionary grants...."

This authority is sufficient to allow "urgent needs" to be funded from the Secretary's discretionary fund.

Reasons to Extend the Urgent Needs Fund

-- The phasedown in hold-harmless will leave many cities with insufficient funds to bring their urban renewal projects to a point where a closeout agreement with the Federal Government could be completed.

-- With the hold-harmless phaseout, the Administration's failure to provide an urgent needs fund may result in authorization of a special urban renewal fund or continuation of hold-harmless.

-- Neither the SMSA discretionary balance nor the Secretary's discretionary fund contain enough funding to meet the urgent needs requirements.

Reasons Not to Extend the Urgent Needs Fund

-- The longer a separate urgent needs fund continues to exist, the longer many cities will delay reaching a final urban renewal closeout agreement. If these separate funds will be available over several years to complete old categorical projects, what incentive is there to pursue an early project closeout?

-- By placing urgent needs funding within the total amount available for all CDBG recipients, communities will be pressed much harder to justify their urgent needs funding as they will be competing against other recipients, who believe they have an equal right to those funds. Further, other recipient pressure will make it very difficult for HUD or the urgent needs applicants to justify any funding beyond the point where it is absolutely essential. There is less chance of "urgent needs" becoming a permanent institution.

HUD Request: Alternative #1. A $100 million urgent needs fund in 1978 is necessary (1) to meet legitimate needs of cities which are losing funding as a result of the hold-harmless phaseout, and (2) to ward off congressional action extending hold-harmless permanently or establishing a separate, categorical urban renewal fund.

OMB Recommendation: We have been given no information whatsoever to either confirm or refute the validity of extending the urgent needs fund. However, we are opposed to continuation of a separate urgent needs fund. If there is a need for special assistance, we would recommend that it come from within the total CDBG funding.

This issue will be discussed further after we receive the Secretary's recommendation for the formula.

SUBISSUE C: Formula Changes

Statement of Issue

What changes, if any, in the CDBG formula should be recommended?

Analysis

CDBG funds are currently allocated by a formula consisting of 25 percent population, 25 percent housing overcrowding, and 50 percent poverty. HUD is considering revising the formula to include one or more additional factors, as well as changes in the weights assigned to each factor. In doing so, HUD's basic objectives are to (1) find factors where data are available; (2) make the least change in the formula necessary, as this will present the least political problem; and (3) put more money into the older cities in the Northeast and Midwest.

The Department is focusing its attention on two new formula elements.

Age of housing. HUD is attempting to define a more specific goal for the CDBG program and devise a formula which will achieve the Department's primary objective: to direct more funds to older, declining cities.

Many of these older cities will be losing a portion of their funding in the years ahead because (1) hold-harmless will be phased out, and (2) the incidence of housing overcrowding in central cities has decreased from 1.8 million to 1.2 million units. HUD maintains that the older cities are already getting less than their fair share because of a weakness in the current formula elements: The poverty index currently used is a standard national figure. It is not adjusted to reflect cost-of-living variations. Thus, the data used in the formula calculation reflecting the number of persons whose incomes are below the poverty level are not an accurate measure and tend to unfairly favor those geographical areas with a lower cost of living.

According to HUD's preliminary findings, adding the element "number of housing units built before 1939" to the formula benefits the older, core cities in the Northeast and North Central areas, where approximately 53 percent of the houses were built before 1939, relative to the South and West, where only 30 percent of the structures fit this criterion. HUD maintains that age of housing correlates closely with density, housing abandonment, and substandard housing, and serves as a proxy for government repair and maintenance costs of older sanitation facilities and sewage lines. Density is a factor associated with urban blight and the more intense use of public facilities.

While inclusion of this element in the formula would offset part of the older cities' loss due to hold-harmless phaseout, the Department believes that certain key cities with greater needs may require further assistance beyond just restoration of part of their loss from hold-harmless phasedown. Additional measures which HUD would take to help these cities include:

-- Distributing funds freed up as a result of the hold-harmless phasedown among all metropolitan cities, but using a special formula based solely on the age-of-housing stock.

-- Creating a priority discretionary fund out of hold-harmless savings which would be awarded to qualifying communities for the purpose of implementing specific plans to eliminate or retard the unique hardships of older cities. This option relates funds to performance.

<u>Cost of housing</u>. As mentioned earlier, the "poverty" figure currently used in the formula is a standard national figure which does not recognize variations in cost of living. However, no data currently exist that would allow for regional variations in poverty levels.

HUD believes if even one major component of the cost of living could be introduced into the poverty factor, the situation would be an improvement over the current national definition. The Department has explored several data sources in this regard:

- BLS family budgets
- BLS CPI for cities
- Fair market rents for section 8-assisted housing
- Actual housing cost in HUD-assisted housing
- Median incomes.

Of these, only the "cost of housing" seems to hold any promise. Actual housing costs incurred in producing HUD-assisted housing around 1969-70--when there was a significantly high volume of production of public housing (conventional and leased), section 236, and rent-supplemented units--could be utilized. Data would be referable to the same point and period of time as the poverty counts in the 1970 Census. 80 Percent of all metropolitan entitlement cities have had some experience with HUD-assisted housing programs so that it would appear possible to compute national average cost for a two-bedroom unit and develop an index for each such city.

HUD is in the process of exploring the overall cost, technical validity, and potential impact of this assumption.

Arguments for Changing the Formula

Inadequacy of present criteria:

-- While population identifies city size and the poverty element can be said to represent the target population which the CDBG funds are principally intended to serve, the overcrowded housing factor is generally not considered to be a good indicator of the housing stock quality. Also, a HUD study indicates that it is not an effective proxy for slums and blight.

-- The national poverty standard used in the formula is not an accurate measurement of actual conditions in specific areas.

-- Even if the poverty measurement can be improved, it is still not a completely accurate measure and should not be weighted so heavily in the formula.

-- The CDBG program is not a poverty program. Its main purpose is not to bolster the financial condition of cities with large poverty populations, but rather to address the problem of physical decay, irrespective of population income levels.

Advantages of the proposed factors:

-- Because CDBG funds can be used for housing rehabilitation, and have been to an impressive degree in the first 2 program years, an indicator reflecting housing condition would be beneficial for inclusion in the formula. "Age of housing" represents a suitable proxy for housing in need of rehabilitation.

-- A formula revision which would weight the program more specifically in the direction of "neighborhood improvement" would provide a closer link between CDBG and other HUD programs. It would also serve as a further indicator of the Secretary's--and the Administration's--commitment to do something about preserving our older cities and their ethnic neighborhoods.

Arguments Against Changing the Formula

-- The "age of housing" element proposed by HUD does not distinguish between low-/moderate-income housing and upper-income housing. Many very old neighborhoods are populated by upper-income residents who can afford to pay sufficient taxes to cover the cost of upgrading or maintaining older support facilities. Also, these people can afford to upgrade and maintain their own homes without Government-subsidized loans or grants.

-- Including an age of housing in the formula would move CDBG closer towards a housing assistance program, thereby making indistinguishable the need for separate CDBG and housing assistance block grant programs.

-- Any proposal to change the formula exposes it to changes that we might not favor, including a permanent extension of hold-harmless if Congress believes it must do something but can't come to agreement on any new ideas.

-- Using a "cost of housing" factor may benefit cities which have strong unions or which have perpetuated obsolete building codes, etc., while penalizing those cities that have more control over the local situation.

-- De-emphasizing poverty in the formula makes the program more regressive by directing funds away from concentrations of low-income population into areas where income is likely to be higher.

-- While the 1974 Act provides a laundry list of objectives of the CDBG program, no one specific focus can be identified as the <u>key</u> objective. Since the eligible activities which can be financed with CDBG and General Revenue Sharing are very similar, it is questionable as to whether CDBG should be continued as a separate entity or folded into a general revenue sharing program. A more narrowly defined formula away from basic population/poverty conditions will make the merging of CDBG with a revenue sharing program more difficult.

-- A change in the formula may create new hold-harmless demands.

HUD Request: None received.

OMB Recommendation: The current poverty definition is an imperfect measurement. This, coupled with the fact that it is the most influential factor in the formula, provides a sound theoretical basis for attempting to perfect this element. Although OMB has not received a specific recommendation from the Department, we believe any improvement that could be made in the poverty element by introducing some index of housing costs should be given careful consideration.

SUBISSUE D: Other Changes

Statement of Issue

What other changes in the CDBG program should be proposed?

Analysis

(1) Nonmetropolitan discretionary balance. HUD will turn this program over to the States for administration. This may be accomplished without a change in the legislation, depending on the Department's specific plan.

(2) Secretary's discretionary fund. The Department will probably recommend deleting innovative projects and disaster relief as eligible activities for CDBG funding. Innovative projects may be financed from HUD's research budget, and communities needing disaster assistance may receive it from the Federal Disaster Assistance Administration.

HUD Request: None received.

OMB Recommendation: No final recommendation, although we would concur with the tentative actions discussed in the paper.

#8. REHABILITATION LOANS

Issue Paper
Department of Housing and Urban Development
1978 Budget
Issue # 8: Rehabilitation Loan Fund

Statement of Issue

Should the authority to make new loans under the Rehabilitation Loan Program be continued beyond 1977?

Background

The Housing and Community Development Act of 1974 provided for termination of the Rehabilitation Loan Program on August 22, 1975. Subsequent legislation, initiated by Congress, has extended the program, and it is now scheduled to terminate at the end of fiscal year 1977. The 1977 appropriation of $50 million, together with a carryover balance of $61 million and estimated repayment income of $37 million, would provide for up to $148 million in new loans during this fiscal year. HUD believes it does not have the capability to obligate this entire $148 million during 1977 but instead estimates a 1977 obligation level of $85 million and a 1978 obligation level of $103 million -- $63 million of carryover from 1977 and $40 million in 1978 repayment income. However, the Department is not proposing a deferral to lock itself into these specific program levels.

Alternatives

#1. Propose legislation extending the rehabilitation loan authority through fiscal year 1978, allowing for a program of $85 million in 1977 and $103 million in 1978 (HUD request).

#2. Allow the authority to terminate after 1977, as currently provided for in law.

#3. Terminate the program in mid-1977 and propose rescission of the unobligated balances (OMB recommendation).

Analysis

Obligations/Outlays ($ in millions)	1976 OBS.	1976 O	1977 OBS.	1977 O	1978 OBS.	1978 O	1979 OBS.	1979 O	1980 OBS.	1980 O	1981 OBS.	1981 O	1982 OBS.	1982 O
Current Policy	39	23	--	-22	--	-29	--	-29	--	-29	--	-29	--	-29
Change from current policy:														
Alt. #1 (Agency req.)	--	--	+85	+61	+103	+86	+35	+25	+35	+15	+35	+10	+35	+5
Alt. #2	--	--	+85	+61	--	+12	--	-8	--	-8	--	-8	--	-8
Alt. #3 (OMB rec.)	--	--	+50	+48	--	-5	--	-5	--	-5	--	-5	--	-5

HUD's request for extension of the Rehabilitation Loan Program is based on several arguments:

-- While communities have been programming substantial amounts of their CDBG funds for rehabilitation finance, they are finding that it takes a longer period of time to develop the necessary administrative capability to operate a rehabilitation program. Section 312 provides an interim means of keeping rehabilitation activities going until the CDBG program becomes operational.

-- The Department does not have the staff capability to obligate the entire $148 million in 1977 alone, and the Secretary would find it most embarrassing if any funds for rehabilitation were allowed to lapse.

-- Section 312 serves as a "little contingency fund for the Secretary" to use in expediting urban renewal closeouts and selling the Urban Homesteading and Neighborhood Preservation Programs.

OMB would dispute these arguments:

-- Communities receiving block grant funds have had three years to develop the administrative capability to operate a rehabilitation program. And a substantial amount of block grant funds are available to finance the expeditious establishment of a rehabilitation program.

-- In 1975, communities programmed $225 million of CDBG funds for rehabilitation activities; in 1976, this amount rose to about $250 million; in 1977 -- $315 million; and in 1978 -- an estimated $379 million. These amounts are far greater than that ever available during any year in the history of the section 312 program. Given the funds programmed for rehabilitation under the community development block grant program, there is no need whatsoever for categorical rehabilitation monies.

-- There is no need for a "contingency fund" to back up the Urban Renewal closeout, Urban Homesteading, or Neighborhood Preservation Programs. Since these are all joint Federal-local efforts, they offer a perfect opportunity to utilize community development block grant funds as the local portion of the joint effort. There is no reason the Secretary should need an incentive fund to sell these worthwhile -- or mandatory -- undertakings.

There has been strong congressional pressure to keep the section 312 program alive. Administration efforts in previous years to hold down the appropriation for the section 312 program or rescind the funds and otherwise terminate the program have been unsuccessful. For 1977, a decision was made not to propose a rescission of the appropriation, although no commitment was made to continue the program. If the program is allowed to continue through 1977, under current law it will automatically terminate.

<u>HUD Request</u>: Alternative #1. Although HUD has offered several programmatic reasons for continuing the section 312 Rehabilitation Loan Program through 1978, the key factor appears to be the Department's inability to obligate the funding level in 1977 alone. The Secretary is strongly committed to neighborhood preservation, of which rehabilitation is a key part, and allowing available funding to lapse at the end of 1977 would appear inconsistent with this commitment.

<u>OMB Recommendation</u>: Alternative #3. There is no programmatic justification for continuation of the program through 1977 or into 1978, given the presence and magnitude of the Community Development Block Grant Program. The amount of funding available from this source far outweighs the importance of whether or not all the categorical money available for rehabilitation loans must be spent.

#9. CATEGORICAL PLANNING

Issue Paper
Department of Housing and Urban Development
1978 Budget
Issue # 9: Categorical Planning/Management Assistance Programs

Statement of Issue

Is there a need for any planning/management programs outside of the Community Development Block Grant (CDBG) Program?

Background

Section 701 of the Housing Act of 1954 authorizes the Comprehensive Planning Grants ("701") Program. Grants may go to States, local governments, areawide organizations, Indian tribes, and other organizations to undertake the following activities:

-- Development of a comprehensive plan.
-- Development of a policy-planning-evaluation capacity.
-- Determination of community needs, with the setting of long-term goals and short-term objectives.
-- Development of programs and activities to meet these goals and objectives.
-- Evaluation of progress in meeting these goals.
-- Development of the management capability necessary to implement plans.

The 1977 Budget provided $25 million for the 701 program for (1) worthwhile planning which merits funding but does not qualify for assistance under other programs; (2) States and areawide agencies to provide technical assistance for small communities in meeting the requirements of the Community Development Block Grant Program; and (3) assistance for the recipients in completing the land use and housing plans required by the Housing and Community Development Act of 1974 in order to be eligible for future 701 funding. An extension of the appropriation authorization for 701 will be needed for 1978 and 1979.

Section 811 of the Housing and Community Development Act of 1974 authorizes "the provision of technical assistance to communities, particularly small communities, to assist such communities in planning, developing, and administering Community Development Programs pursuant to Title I of the Housing and Community Development Act of 1974." Appropriations for this activity are authorized without regard to dollar or fiscal year limitations. The Administration has never requested funding for this section nor has the Congress provided it.

Section 105 of the Housing and Community Development Act of 1974 authorizes the use of CDBG funds by States and local governments for the following planning/ management activites:

-- Development of a comprehensive community development plan.
-- Development of a policy-planning-management capacity.
-- Determination of community needs, with the setting of long-term goals and short-term objectives.
-- Evaluation of progress towards meeting these goals.
-- Management, coordination, and monitoring of activities necessary to implement plans.

In both the 1976 and 1977 House Reports on the Appropriations Acts, HUD was directed to urge the use of CDBG funds for these purposes, especially by entitlement communities receiving annual funding, as a substitute for 701 funding. The Department estimates that during 1978, local governments will use about 3 percent of the total CDBG funds--or $100 million--for planning and management activities.

<u>Alternatives</u>

#1. Provide $80 million for the 701 program and $15 million for a separate CDBG technical assistance program (section 811) in 1978 (HUD request).

#2. Continue the 701 program at the $62.5 million level but provide no funding for technical assistance outside the CDBG program.

#3. Provide $25 million for the 701 program in 1978, consistent with the 1977 Budget, but no funding for technical assistance outside the CDBG program.

#4. Provide no funding for categorical planning/management programs outside of the CDBG program (OMB recommendation).

Analysis

Budget Authority/Outlays ($ in millions)	1976 BA	1976 O	1977 BA	1977 O	1978 BA	1978 O	1979 BA	1979 O	1980 BA	1980 O	1981 BA	1981 O	1982 BA	1982 O
Current policy (Alt. #2)	75	94	63	100	63	55	63	63	63	63	63	63	63	63
Change from current policy:														
Alt. #1 (Agency req.)			---	---	+32	+14	+32	+29	+32	+32	+32	+32	+32	+32
Alt. #2			---	---	---	---	---	---	---	---	---	---	---	---
Alt. #3			---	---	-38	-7	-38	-30	-38	-38	-38	-38	-38	-38
Alt #4 (OMB rec.)			---	---	-63	-12	-63	-50	-63	-63	-63	-63	-63	-63

For 1978, the Department is requesting $80 million for the 701 program. The $80 million level is described as a continuation of the 1976 appropriation of $75 million plus $5 million to cover the impact of inflation. HUD's justification ignores both the $25 million 1977 program level requested in the President's budget and the final appropriation of $62.5 million.

The 1978 701 funds would be allocated as follows:

$21.5 million	States
32.0 million	230 Metropolitan Areawide Organizations
12.0 million	350 Nonmetropolitan Areawide Organizations
12.0 million	750 Localities
1.5 million	90 Indian tribes
1.0 million	Other

The activities to be financed are:

- -- Development and refinement of State-regional housing and land use plans and develoment of programs to implement these plans.
- -- Development of comprehensive plans.
- -- Addressing of other State and local land use and housing priorities.
- -- Increasing the capability of areawide planning organizations to assist communities in coping with the CDBG program.
- -- Improving the A-95 process.
- -- Making studies and publishing information on comprehensive planning and related management problems to enable States, areawide organizations, and local governments to increase their capability.

The Department is also requesting for 1978 $15 million to establish a new CDBG technical assistance program. HUD did not request funding of this program when the CDBG program was first established (1) for fear of continuing by the back door the same Federal control which CDBG was trying to eliminate, (2) because entitlement cities could and did use their CDBG funds to purchase their own assistance, and (3) because 701 could and did provide such assistance. However, HUD does not believe these methods have been sufficient. In the first 6 months of this year, HUD monitoring uncovered 3,667 instances of program "abuse," two-thirds of which was in entitlement communities and one-third in discretionary communities. The five most prevalent program abuses were in the areas of equal opportunity, relocation/acquisition, environment, labor standards, and citizen participation. Without Federal assurance of assistance to cities experiencing problems, HUD fears it will face demands for more front-end review and more situations in which small, needy communities are excluded from the program for failure to perform. Examples of the kinds of activities the technical assistance program will fund are:

- -- Disseminate knowledge and experience to groups of communities needing them to meet program requirements or make best use of program opportunities.

-- Provide individual assistance to small-town recipients with no other CDBG funds available. An example is a talent pool organized by a State municipal league in which a staff member from a city which has successfully completed environmental reviews is paid to go help a different city which needs such experience.

Technical assistance monies will not be used to--

-- Fund city payrolls by paying staff of a city to help itself.
-- Provide intensive long-range assistance to individual cities that have annual CDBG grants (even though the incidence of abuses was far higher for these cities).
-- Undertake research projects.

The Secretary may contract with any public or private organization, including any of the eligible 701 or CDBG recipients, to provide CDBG technical assistance. Although the amount is not specified, the majority of the funds will be directed toward metropolitan areas.

The 701 program and the proposed CDBG technical assistance program are nearly identical in that:

-- The authorized eligible activities are the same: general comprehensive planning and management and capacity building to cope with Federal assistance and implementation of plans.
-- States, localities, areawide agencies, and private contractors may receive the funds.

The 701 and CDBG technical assistance programs have two major features that are not authorized in the block grant program:

-- They may <u>directly</u> fund metropolitan and nonmetropolitan areawide organizations.
-- States may compete for an unlimited amount of the available funds.

Although States may compete for funds from the SMSA and non-SMSA discretionary balances of the CDBG program, the amount they may receive is limited to the formula allocation available for an area and the funds must be used for that area. States may also receive funds directly from the Secretary's Discretionary Fund. The use of CDBG funds by States for planning/management activities is not specifically authorized. States may not receive CDBG funding to support activities undertaken for their own benefit.

Need for Categorical Planning Program Outside the CDBG Program

Arguments for:

-- 701 Is the only Federal program which can directly fund States, local governments and areawide agencies for the purpose of coordinating the planning and implementation of other Federal assistance at the local level.

-- Areawide agencies and States are not eligible recipients of CDBG funds. Terminating the 701 program would terminate all direct Federal funding of areawide agencies and States for comprehensive planning and management activities. Nor would either group be able to fulfill the key role they would surely have in a technical assistance program.

-- CDBG recipients are under pressure to use their CDBG funds for visible public projects and cannot use all the funding they may need to conduct important planning activities.

-- CDBG discretionary recipients do not receive continuous guaranteed funding but instead only 1-year grants. This does not provide the base necessary to establish an on-going planning process or system of technical assistance.

Arguments against:

-- There is no activity of either the 701 or a CDBG technical assistance program that is not authorized to be undertaken with CDBG funds.

-- If any planning/management assistance is considered a high priority activity, repetitive CDBG funding may be granted to establish a continuous process.

-- The original purpose of categorical planning programs--to encourage hesitant local governments to undertake planning that would otherwise not be done--is outdated; local governments today possess the interest and the capability to undertake planning in areas they consider important.

-- Section 302 of the Intergovernmental Cooperation Act of 1968 authorizes a better mechanism for getting technical assistance to other levels of government: "The head of any Federal department or agency is authorized within his discretion, upon written request from a State or political subdivision thereof, to provide specialized or technical services, upon payment, to the department or agency by the unit of government making the request, of salaries and all other identifiable direct or indirect costs of performing such services...."

-- Section 402 of that same Act attempts to direct Federal fund to elected officials who will determine their use: "Where Federal law provides that both special-purpose units of local government and units of general local government are eligible to receive loans or grants-in-aid, heads of Federal departments and agencies shall, in the absence of substantial reasons to the contrary, make such loans or grants-in-aid to units of general local government rather than to special-purpose units of local government." Funding of areawide orqanizatons with 701 or CDBG technical assistance monies in lieu of State and local governments, conflicts with this major policy.

-- The major recipients of categorical planning assistance are the metropolitan areawide agencies, whose members all receive annual CDBG entitlement funding which may be used for planning/management activities.

-- Although areawide agencies do not receive direct CDBG funding, they may receive planning/management assistance indirectly under the CDBG program via participating cities.

-- Establishing planning and implementation funds for one program from one funding source assures that planning will be directed towards specific implementation problems and will be funded only to the extent necessary to reach those goals. The possibility of funding planning just for the sake of planning will be less likely to occur than if planning were funded from an independent source and its progress or value judged independently.

HUD Request: Alternative #1. HUD believes that continuation of the 701 program and a technical assistant program are essential if it is to meet its three objectives: (1) provide recipients with the resources necessary to devise programs to implement their comprehensive, housing, and land use plans; (2) provide CDBG technical assistance; and, (3) allow recipients to continue their own comprehensive planning activities. Limiting planning funding to only CDBG recipients would terminate all direct Federal support of areawide agencies, which provide an essential service in assisting CDBG recipients to prepare and implement their housing assistance and community development plans.

OMB Recommendation: Alternative #4. HVLD continues to believe there is no programmatic justification for the 701 program. Those areas receiving the majority of the 701 funds are already receiving the majority of the CDBG funds. Further, we believe the funding of areawide agencies should come from their members--the local governments -- to assure that areawide efforts are directed toward meeting the needs of local governments. It is of no benefit to the Federal Government to continue providing independent funding to the areawide groups when there is no assurance that this funding will result in plans that local governments will implement.

We would also note that any of the local governments, or States on behalf of local governments, receiving CDBG grants may use their funds for technical assistance. However, if the Department believes there is a need for more CDBG technical assistance or that the allocation for any one area is not sufficient to meet the need for technical assistance, we would have no objection to amending section 107 of the 1974 Act to allow State and local governments to also receive monies from the Secretary's Discretionary Fund in order to develop, purchase, or provide CDBG technical assistance. In this way, we will not be establishing another independent program which is likely to become institutionalized in its own rights. If the technical assistance funding comes from the same sources as implementation funding, it is likely that technical assistance will be funded only so long as it is needed. Funds would then be diverted to implementing the program.

#10. DEPARTMENTAL MANAGEMENT

Issue Paper
Department of Housing and Urban Development
1978 Budget
Issue #10: Departmental Management

SUBISSUE A: Staffing

Statement of Issue

What should be HUD's 1978 staff level?

Background

In recent years, HUD employment has fluctuated because of programmatic and organizational changes. The high point was 15,820 full-time permanent (FTP) employment in 1973; the low was 14,942 FTP in 1976. OMB estimates for 1977, 1978, and 1979 are within this range.

A majority of the Department's staff costs is attributable to the activities of the FHA Fund. A transfer from the FHA Fund to "Salaries and Expenses, HUD" is approved in appropriation acts. Smaller transfers from the revolving funds of GNMA, New Communities, and FDAA are also made to meet the staff costs attributable to those activities. In addition, fees collected by the Department go to meet staff costs. The costs not met from these sources require an annual appropriation. In 1976, of the total obligations of $408 million for staff expenses, $171.1 million was appropriated and the remaining $236.9 million came from the FHA Fund, other revolving funds, and fees.

The 1977 Budget requested 15,650 FTP positions and 17,275 total positions. Congressional cuts reduced those numbers to 15,570 and 16,890, respectively.

Alternatives

#1. Approve ceilings of 16,870 FTP and 18,170 total positions in 1978. Approve a supplemental request for 10 positions in 1977 (HUD request).

#2. Approve ceilings of 15,564 FTP and 16,899 total positions in 1978. Reject the 1977 supplemental request (OMB estimate).

#3. Make an arbitrary cut of 1,000 positions in 1978 below the levels based on program recommendations (14,564 FTP and 15,899 total positions).

Analysis

Obligations ($ in millions)	1976 Obl.	1977 Obl.	1978 Obl.	1979 Obl.	1980 Obl.	1981 Obl.	1982 Obl.
Current policy 1/	408	461	473	473	473	473	473
Change from current policy:							
Alt. #1 (HUD req.)	---	2/	+36	+36	+36	+36	+36
Alt. #2 (OMB est.)	---	---	2/	-8	-8	-8	-8
Alt. #3	---	---	-28	-28	-28	-28	-28

Employment (numbers of personnel)	1976 FTP	1976 Total	1977 FTP	1977 Total	1978 FTP	1978 Total	1979 FTP	1979 Total
Current policy.......	14,492	16,400	15,570	16,890	15,570	16,890	15,570	16,890
Change from current policy:								
Alt. #1 (HUD req.).	---	---	+10	+10	+1,300	+1,280	+1,300	+1,280
Alt. #2 (OMB est.).	---	---	---	---	-6	+9	-300	-295
Alt. #3............	---	---	---	---	-1,006	-1,001	-1,006	-1,001

	1980		1981		1982	
Current policy.......	15,570	16,890	15,570	16,890	15,570	16,890
Change from current policy:						
Alt. #1 (HUD req.).	+1,300	+1,280	+1,300	+1,280	+1,300	+1,280
Alt. #2 (OMB est.).	-300	-295	-300	-295	-300	-295
Alt. #3............	-1,006	-1,001	-1,006	-1,001	-1,006	-1,001

1/ Assumes no pay increase impact beyond the October, 1976 increase.
2/ Change of less than $500,000.

HUD has been expanding the coverage of its work measurement system; 73 percent of its requested staff positions in 1978 are covered by this system. By defining discrete work tasks and reasonable time standards for task completion, the work measurement system can estimate staffing impacts resulting from major policy decisions.

Productivity can be tracked by examining changes in standards over a period of years. Both OMB and HUD have used the system to make 1978 staff estimates.

Alternative #1--Approve ceilings of 16,870 and 18,170 in 1978 and a 1977 supplemental for 10 positions in the proposed Energy Conservation Standards Program. HUD's request for an increase of 1,300 FTP positions and 1,280 total positions over 1977 levels are based primarily on the Department's program level requests for 1978, although some discretionary increases are requested for parts of the Department not covered by workload measurement. The major components of the increase are:

- 846 Positions for Housing programs.
- 131 Positions for Community Planning and Development.
- 101 Positions for the Federal Insurance Administration.
- 76 Positions for Field administration.
- A decrease of 20 positions for temporaries.

Alternative #2--Approve ceilings of 15,564 and 16,899 in 1978 and reject the energy conservation standards supplemental request for 1977. The OMB-recommended staff levels are based on workload calculations using HVLD program recommendations. (Actual staffing requirements might be slightly higher or lower if HUD did detailed calculations based on HVLD program recommendations.) In addition, some discretionary cuts (about 5 percent of the total) have been made in areas not covered by workload measurement. The major cuts from the HUD request are:

- 740 Positions based on the recommended section 8 level.
- 368 Positions based on termination of Comprehensive Planning Grants and Rehabilitation Loans and proposed changes in Community Development Block Grants which would require States to administer discretionary grants.
- 17 Positions based on the recommended program level for Research and Technology.
- 51 Positions in Field administration support personnel stemming from programmatic cuts in section 8 and Rehabilitation Loans.
- 10 Positions for energy conservation standards both in 1977 and 1978, pending a decision on funding, which is recommended to be provided by a transfer from ERDA to HUD.

The major discretionary cuts in areas not covered by work measurement are:

- 37 Positions in Community Planning and Development.

- 10 Positions for requested special assistants to Regional Administrators, based on PMI emphasis on controlling "assistant to" positions.
- 17 Positions scattered throughout the Department.

In addition, 35 FTP positions requested by HUD for FDAA and Field administration personnel are recommended for temporary positions. The HVLD recommended program levels also result in cuts of 294 FTP and 304 total positions in 1979 when workload calculations are made.

Alternative #3--Make an arbitrary cut of 1,000 below levels based on programmatic recommendations. This option would generate estimated budget savings of $28 million in 1978 and $20 million in 1979 when compared to Alternative #2. This would assist in the effort to balance the 1979 budget. However, the Department would not be able to implement the HVLD-recommended program levels effectively. These inefficiencies might actually increase program costs, certainly in outyears if not in 1978. Further, such a cut would undermine the Department's efforts to rationalize staffing requests by directly tying staff levels to program levels.

HUD Request: Alternative #1. Based primarily on requested program levels, HUD is requesting an FTP level of 16,870 positions and a total level of 18,170 positions.

OMB Estimate: Alternative #2. Based primarily on HVLD-recommended program levels, HVLD estimates HUD would require 15,564 FTP positions and 16,899 total positions in 1978. HVLD-recommended program levels also lead to an estimate of 15,270 FTP positions and 16,595 total positions in 1979.

SUBISSUE B: Automated Data Processing

HUD Request: A 1978 ADP level of $24.1 million and 342 staff positions, an increase of 21 over 1977.

ISD/HVLD Recommendation: A 1978 ADP level of $23.3 million and 321 staff positions.

Discussion

HUD's ADP budget has increased significantly in recent years (doubling since 1975), but the increases appear justified for two reasons: (1) HUD began taking advantage of ADP technology relatively late and (2) a large portion of the increase is attributable to HUD MAP, an integrated, comprehensive accounting and tracking system for FHA insurance operations. HUD MAP development is virtually complete, and test operations will begin in 1977. Significant improvements in meeting FHA objectives are expected when HUD MAP is fully operational. Because the requested staff increase of 21 would be primarily for new systems development, which we consider a secondary priority to HUD MAP and some hardware changes, we recommend against the staff increase. This cut, plus anticipated savings from the Presidential Management Initiatives program, reduce the HUD request by $750,000.