Low Income Housing Preservation Program

Low-Income Housing Preservation & Resident Homeownership Act (LIHPHRA)

October 27, 1995

1) The Current Senate HUD-VA-IA bill;

- The Senate Passed (9/27/95) HUD-VA-IA Appropriations bill funds the Low Income Housing Preservation program at $624 million budget authority and zero budget outlays.

2) What do tenants need to preserve their housing and prevent being displaced?

- To Preserve low-income housing at affordable rents and to prevent displacing tenants, the Senate has the options below:

what does this fu

Senate options to Preserve Housing & Protect Tenants:	Budget Authority	Budget Outlays
Option #1 New LIHPHRA "Capital Grant"	$624 million	$440 million
Option #2 Amend current LIHPHRA "Capital Grant"	$791 million	Zero

Everything

#3 $758 ① queue

$1.1 B | Zero | ② Sales in pipeline

Everything

3) What should the Senate do?

- Based on the Senate's VA-HUD-IA bill, the Senate has the following choices;

1) Fund $440 million in Outlays.

OR

2) Fund $176 million more in Budget Authority (new total: $791 million)

4) If the Senate does not amend the HUD-VA-IA bill;

- Thousands of seniors, disabled, and low-income families face displacement and may become homeless.
- Congress will then have to decide "who should we throw out of their homes"

October 27, 1995; National Low Income Housing Coalition: 202/662-1530 (w) 202/393-1973 (f)
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TO: Molly Broastorm
Senior Policy Analyst
202-456-7028

DATE: 12/21/95

FROM: Michael Kane

Number of pages included in this fax:__________

Comments:

Attached please find
NAHT Fact Sheets on the "Voucher" Plan
and "Mark-to-Market" proposal.
Also NAHT press release
Letter requesting meeting
w/ NAHT tenant representative
w/ Panetta, Ickes + other
White House staff is forthcoming

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HUD TENANTS CLAIM VICTORY IN CONGRESSIONAL HOUSING VOTE, URGE CLINTON TO UPHOLD TENANT GAINS

Contact: Michael Kane or Karla Armenoff, 617-267-9564
Embargoed for release: Until final action by House and Senate on HUD Appropriations Bill

Millions of families in privately-owned, HUD assisted housing are poised to win a temporary reprieve from threats to their homes if this week's Housing Appropriations vote is upheld by President Clinton, according to the National Alliance of HUD Tenants (NAHT). NAHT, a rapidly growing membership organization of tenants in HUD, multifamily housing successfully lobbied to win back funds and protections for tenants which had been cut back in earlier actions by Congress and the Clinton Administration.

"Over 4.5 million low income families have been saved, for now, from an increase in rents from 30 to 32% of income in subsidized and public housing," stated Cynthia Reed, a Chicago tenant and President of the NAHT Board. The House had earlier voted for this rent increase for 3 million Section 8 tenants in privately-owned housing, and the Senate had previously allowed housing authorities to roll back the 'Brooke Amendment' for 1.5 million public housing families as well. "This week's vote showed that Congress has heard the voices of millions of tenants who will be squeezed too much by other cutbacks in health, welfare, jobs, education and by tax increases for the poor," added Reed.

Reed also noted that NAHT was successful in getting Congress to strike language allowing the Administration to implement its controversial "Voucher Plan" to convert all expiring project-based Section 8 contracts into vouchers for a smaller number of tenants. "NAHT has led the fight against the Clinton Voucher Plan for over a year because it is a costly and dangerous experiment which will displace hundreds of thousands of families and destroy affordable housing," stated Reed. "While we applaud this change in the Appropriations bill, we recognize that both Congress and the Administration plan to revisit the Voucher Plan early next year. We call on President Clinton to withdraw his voucher plan and on Congressional leaders to put it to rest once and for all."

NAHT and its local affiliates staged Save Our Homes rallies in 26 cities last year opposing the Clinton Voucher Plan. In February, NAHT demonstrators delivered a giant Voucher to "Resident Clinton", the nation's most public housing tenant, at a widely-publicized White House rally. Reed vowed that NAHT affiliates would redouble their efforts next year until the plan is defeated.

NAHT Board member Carol Berman, a tenant from the Countywide Alliance of HUD Tenants in Los Angeles, also praised the vote by Congress to authorize up to $744 million for the embattled Title VI Preservation program. "These funds will preserve housing for 40,000 families who would otherwise lose their homes," stated Berman. "Most of these families will also gain control over their communities through resident or nonprofit ownership, which gets priority under the bill. This is a major victory for NAHT and its allies, since the Clinton Administration had sought zero funding for Preservation and the final amount is higher than either house had voted for last summer."

Added NAHT Board member Sylvia Evans of the Plaza Neighbors Association for Portland, Oregon, "At the same time, we are concerned that thousands of other low income families will lose their homes due to passage by Congress of an amendment--proposed by the Clinton Administration-- which will allow subsidized housing owners to prepay their mortgages and raise rents to market levels. This shows that the fight to save our homes is far from over."

"Our struggle now shifts to the White House," stated NAHT Board member Lucy Johnson from the Greater Syracuse Tenant Network and the New York State Tenant and Neighborhood Information Service. "For the last year, the White House has led an all-out assault on the nation's affordable housing system with proposals to defund, deregulate, and voucherize our homes. Tenants have had to rely on Republican moderates in the Senate to hold the line. In particular, we appreciate the leadership shown by Senators Bond, D'Amato and Mack in saving the Preservation program and slowing down the Administration's drive to raise rents and voucherize."

NAHT leaders are concerned that the White House may try to bargain away the Preservation program in order to fund other Administration priorities in the VA/HUD/Independent Agencies Appropriations bill, which Clinton has vowed to veto because of cutbacks to Americorps and the EPA. An earlier Administration attempt to do this in the Senate was rebuffed by intense tenant lobbying two months ago. "Tenants across the country fought long and hard to win back funds for the Preservation program, which the Administration has been trying to kill. We ask President Clinton to hear our voices and uphold the Congressional vote to save our homes," stated Reed. "We do not want to see Housing Preservation become the 'sacrificial lamb' in budget negotiations over other worthy domestic programs," added Berman.

The NAHT Board also released a letter to the White House requesting a meeting with Chief of Staff Leon Panetta to discuss tenant demands to preserve the Preservation Program, withdraw the Voucher Plan, and to drop the deregulation and rent increases proposed in HUD's controversial "Mark to Market" scheme.

Other NAHT tenant leaders and local affiliates are available for comment in most regions of the country. Contact Michael Kane or Karla Armenoff at the NAHT office at 617-267-9564 for information on how to contact them.

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SAVE OUR HOMES DAY

Talking Points on Project-Based Section 8 & Public Housing

JUST SAY NO TO CLINTON'S VOUCHER PLAN

* ***The plan to replace Public Housing and Project-Based Section 8 with Vouchers will destroy affordable housing.*** President Clinton wants to phase out all public housing and project-based Section 8 subsidy programs. He wants to replace this housing with rent vouchers for individual tenants, who could decide to stay or move. Ending the public housing operating subsidies and Section 8 contracts means much of the nearly 3 million units of this housing will deteriorate, as some tenants move out. Tenants who can't find available housing elsewhere--large families, minorities or the elderly--will be left behind in deteriorating buildings, while operating subsidies to owners are cut. Still other units in high market areas will be lost as owners "gentrify" buildings. Either way, the President's proposal will destroy our homes and our communities.

* ***Vouchers will mean homelessness.*** Vouchers are 20% more expensive per unit than public housing and project-based Section 8. The President is proposing to cut, not increase HUD funding, so vouchers mean that at least 20% of tenants of project-based Section 8 and public housing will be displaced. As many as 500,000 families could be made homeless by Clinton's voucher plan. Even more will be displaced if Clinton and/or Congress cut funds below current levels.

* ***Block grants slash housing funding and aid fewer tenants.*** The Clinton plan does not guarantee vouchers to all current public and subsidized housing tenants. Instead, Clinton proposes to consolidate public housing and Section 8 subsidies into a block grant to the states--at much lower funding levels. It would be up to the states to decide which public and subsidized housing tenants would be able to get vouchers. After the housing subsidies are "block-granted" and tenants scattered, it will be easier for Congress to cut funds even more and harder for tenants and communities to resist.

* ***Vouchers don't mean decent, affordable housing.*** Unlike public housing and project-based Section 8, vouchers don't necessarily guarantee affordable rents for tenants. When a low-income tenant has a fixed-rent voucher, a landlord wants to charge as much as he or she can get. But in public housing and project-based Section 8, rents are guaranteed to be affordable to low-income tenants. In many markets, tenants with vouchers are unable to find decent housing due to lack of available units, discrimination, moving costs, access to transportation, or high rental costs.

* ***Public Housing and Project-Based Section 8 provide low-income housing for a diverse range of Americans. We cannot afford to lose this housing.*** There are more than 1.4 million units of public housing and over 1.5 million units of project-based Section 8 in the country. People in urban, rural, and suburban communities live in this housing. Hundreds of thousands of these units are set aside for senior citizens, people with disabilities and formerly homeless people. Once lost, these units will be extremely hard to replace.

* ***Public Housing and Project-Based Section 8 provides better-quality housing than the private***

real estate market. 25% of low-income housing on the private market is substandard (Harvard University Joing Center on Housing), while only 7% of project-based Section 8 (HUD Policy Development and Research Division) and 6% of public housing (National Commission on Distressed Public Housing) is substandard. While some public and project-based Section 8 housing needs major improvements, vouchers eliminate the best protection tenants have for decent housing--a contract with HUD they can use to enforce housing quality standards. With vouchers, tenants lose this contract and its protections.

* ***Vouchers don't really save money.*** Real cost-savings for the federal government can come from refinancing the project-based Section 8 buildings, which is one piece of the President's housing proposal we can support. In addition, there are tremendous savings available through cutting widfall profits given to owners under some HUD multifamily housing programs.

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Mark-to-Market: HUD's Radical Proposal to End HUD-Assisted Housing Programs

Mark-to-Market: An Out of Control Proposal? Mark-to-Market is a concept which mushroomed from two paragraphs with no detail in the December HUD "Reinvention Blueprint" into the most far reaching proposal affecting federal housing policy for the past three decades and perhaps for the next three decades.

What Housing Would be Affected? HUD provided mortgage insurance and interest rate buydowns to the banks which loaned the money to build this housing. The FHA mortgage insurance means the banks did not have to take any risk because if the owner defaults HUD will bail them out. The buildings which would be Marked-to-Market have Section 8 contracts which provide a guaranteed income stream for the owners. If you live in a Section 236 or Section 221(d)(3) development with a Section 8 contract or in a Section 8 New Construction or Section 8 Substantial Rehabilitation, your homes would be Marked-to-Market under HUD's proposal. If you live in any development with a Section 8 contract, or any development with FHA-insurance, the outcomes of Mark-to-Market could define the future of your housing.

Mark-to-Market Means Restructuring Debt Mark-to-Market, when first proposed by HUD last December, involved restructuring the FHA-insured mortgages by putting the building into default and using FHA-insurance funds to make a big (multi-million dollar) payment on the principal. The result would be a significant reduction in monthly operating expenses which would mean that inflated rents could be lowered significantly because less income would be needed to meet monthly operating expenses.

Reducing Inflated Rents Originally, the concept of Mark-to-Market was favorably received by tenant groups because the idea was to reduce the grossly inflated Section 8 rent levels to true market rents to save HUD money. HUD needs to find ways to save money and project-based Section 8 is the number one target in Congress.

Mark-to-Market & Vouchers HUD's Mark-to-Market plan also includes HUD's proposal to turn project-based Section 8 into tenant vouchers. There is nothing about Mark-to-Market which must be linked to vouchers. Mark-to-Market cost savings could be had without turning project-based funding into vouchers.

Mark-to-Market & Rent Increases In Section 236 and Section 221(d)(3) buildings where rents are frequently more affordable than the private market, HUD's newest Mark-to-Market proposal would actually raise the rents to market levels. This saves no money and will actually increase HUD's costs.

The End of HUD-Assisted Housing Mark-to-Market as is being currently proposed would end long-range Section 8 contracts and replace them with one year vouchers. Mark-to-Market would also eliminate the FHA-insured mortgage in these buildings and with it the Section 236 and 221(d)(3) interest subsidy. This means buildings which are Marked-to-Market would no longer be regulated by HUD at all. They would become private market rentals where owners could do whatever they please--including conversion to high-income condos or demolition! Tenants' rights to go to HUD and get HUD contracts and regulatory agreements enforced would be gone because there would no longer be any contracts or regulatory agreements in this housing.

The Politics of HUD-Reinvention HUD is pushing the Mark-to-Market plan and Congressman Lazio of New York (Suffolk County) is expected to introduce a bill which includes Mark-to-Market. Members of the Senate Banking Committee and its Housing Subcommittee have raised strong objections to Mark-to-Market. Senators Kit Bond, Alfonse D'Amato and Connie Mack have played particularly key leadership roles in raising these objections. But all of the Senators on the Housing Subcommittee, from both parties, raised objections.

Special thanks to Billy Easton, New York State Tenant & Neighbors Coalition for drafting the Facts Sheet.

THE AFFORDABLE HOUSING PRESERVATION PROGRAM

Prepared for the Los Angeles Countywide Alliance of HUD Tenants

FACT SHEET AND CURRENT STATUS OF HUD APPROPRIATIONS

October 18, 1995

The following is a description of the agenda supported by the Los Angeles County-wide Alliance of HUD Tenants and the National Alliance of HUD Tenants.

What Buildings are we talking about here anyway?: The Federal government subsidizes housing for low income people under many different programs. Public Housing generally refers to large developments built with Federal funds given to Public Housing Authorities (cities and counties and states). There are also vouchers and certificates given to individual tenants under the Section 8 program. Finally, there are various other programs including the Section 236 and Section 221(d)(3) Programs where funds are given to private nonprofit and for profit developers to build affordable housing.

What is the 236 or 221(d)(3) Program: In the mid 1960s and early 1970's approximately 1.5 million units of affordable housing were built under these two federal programs which are named after the Sections of the law that created them.

What Keeps Rents Affordable in these buildings?: Rents are kept affordable in large part because the housing was built with a 1% interest loan from the government. In exchange for getting this very low interest loan, the owners agreed to rent to lower income people for 40 years OR after 20 years the owner can pay off what he or she owes to the government and convert to market rents.

In some developments, the low interest loan was not enough to keep rents affordable. HUD allowed rent increases to pay for increased operating expenses (utilities, minor repairs, security, etc.). Rents sometimes rose above what very low and low income tenants could afford. The government added a Section 8 subsidy which is attached to the unit (referred to also as project based Section 8 or Loan Management Set Aside). Low and very low income tenants pay 30% of their income. The Section 8 covers the difference between the tenant's contribution and what HUD has decided it costs to run the development.

Why do we need a preservation program?: 20 years after the development was built, the owner can pay off what he or she owes to the government and convert to market rents. The government cannot take this right away from the owner without compensating the owner. To address the threat of mass prepayment, in 1990 the Congress passed the Low Income Housing Preservation and Resident Homeownership Act (LIHPRHA), which provides opportunities for tenants and nonprofits to purchase the buildings if the purchaser agrees to keep the units affordable for another 50 years. Owners can also opt to remain in the program themselves for another 50 years in exchange for incentives.

Why is the preservation program in danger?: The preservation program is considered costly. Tenants have suggested cost savings ideas. Tenants, owners and the Congress are working on redesigning the program to make it more cost effective. Unfortunately, unless money is appropriated in 1996, we will lose thousands of units to market rate cônversion while the program is being re-designed.

How many units are at risk?: Experts from the National Housing Trust and the California Housing Partnership estimate that there are 140,000 units at risk of market rate conversion nationally. Over 27,000 located in the State of California and 10,500 in the City of Los Angeles. According to the National Housing Trust, a failure on the part of the Congress to appropriate sufficient funds to the Preservation Program will result in a loss to the State of California of over $84 million.

What is congress proposing to do with regard to the Preservation Program?

> **The House of Representatives:** The House has passed a bill that appropriates $200 million for preservation if the program is redesigned and if there are unobligated carryovers (i.e. money unspent from the 1995 budget) from the Annual Contributions Account (an account used for public housing developments).
>
> **The Senate:** The Senate has passed a bill that funds the costs of buying out the owner's right to prepay with a Capital Grant instead of a loan. In order for an owner to participate in the new program, he or she must have at least $5000 in equity in each unit (on the theory that owners with less equity than that will not prepay). The Senate proposal imposes a cost limit equal to the Fair Market Rents for the area x 60 months (as a cost savings measure). These three factors (a grant instead of a loan, equity floor and cost limit) save money in the long run. Unfortunately, the re-designed program is more expensive in the first five years, because most of the costs are paid in year one and the rest of the costs are paid in years two through five (unlike a loan program where the costs are spread out over the 50 year period). Although the Senate is appropriating sufficient funds over a five year period (Budget Authority), none of these funds can be spent in FY 1996.
>
> The Senate's proposal has some elements that tenants are happy with including:
>
> 1. Incentives to facilitate sales;
> 2. $20 million for technical assistance for resident capacity and pre-development;
> 3. The preserved properties will remain affordable for another 50 years;
> 4. Tenants and tenant supported nonprofits will continue being priority purchasers as under old LIHPRHA;

There are, however, problems with the Senate's proposal which put thousands of units at risk. Projects in high market areas (such as California) are particularly vulnerable.

COMPARISON OF THE HOUSE AND SENATE BILLS TO WHAT IS NEEDED IN ORDER TO PRESERVE DEVELOPMENTS IN CALIFORNIA

The following chart compares what is needed to preserve this housing to what the House and the Senate are proposing.

What we need	What the House Did	What the Senate did
Demand #1: $624 million in Budget Authority (total program costs over five years) AND $440 million in outlays (actual expenditures) for FY 1996 (which begins October 1, 1995). The re-designed program must either start on October 1, 1995 or must allow for developments to be processed under the old program until the new program is put into place.	$200 million in outlays if there is money left over from the Annual Contributions Account in 1995 and for a re-designed (more cost effective) program.	$624 million in Budget Authority $0 in outlays for FY 1996
Demand #2: A program that is Mandatory i.e. owners should not have the option of prepaying and charging market rents.	Go forth and redesign the program.	Owners have the option of filing under the new program or pre-paying their mortgages.
Demand #3: A program that allows deals already approved under the old program to go forward i.e. Grandfather sales with approved Plans of Action	Go forth and redesign the program.	HUD has discretion to grandfather if the owner wants to be grandfathered. The tenants have no right to voice an opinion.
Demand #4: Retain LIHPRHA displacement protections: 1) Seniors/disabled get to stay where they are for three years at same rent (plus any HUD approved rent increases they would have gotten anyway); 2) Everyone gets the same thing if you are in a low vacancy area (defined at 24CFR 248.101; 3) If displaced, very low or low income receive a voucher; 4) The owner has to pay 50% of relocation expenses.	Go forth and redesign the program.	1) Very low income people receive a 2 year voucher which could get renewed if there is money in two years; 2) Low income people get $1500 for relocation expenses; 3) Moderate income people get nothing. Technical problem excludes from relocation benefits developments that fall outside thresholds.
Demand #5: An internal rent subsidy to provide further protections to very low income tenants as long as the total cost of the Capital Grant remains within the Federal Cost Limits.	Go forth and re-design the program.	No internal rent subsidy.
Demand #6: Allow local governments to pass laws to address prepayment by removing federal pre-emption in LIHPRHA.	Go forth and re-design the program.	Federal pre-emption remains in the law.

Section 8 Contract Renewals

Tenant groups are also concerned about the renewal of Section 8 Contracts both for the buildings eligible for the Preservation Program and for other buildings. The bill appropriates funding for contract renewals. Tenants will continue paying 30% of their income (compared with the House version which raises tenant contribution to 32%), but:

1. The amounts may not be sufficient; they are combined with expiring certificate and voucher contracts;
2. Due to outlay problem (no expenditures until October 1996), these provisions don't go into effect until October 1, 1996 even though some contracts expire before then;
3. The bill only provides for a renewal for one more year. (This is not a problem if contracts are renewed each year but there are no guarantees);
4. HUD and owner can agree to substitute vouchers without tenant consent;
5. The Senate Committee Report provides only one-time, one-year LMSA Section 8 renewals with a conversion to vouchers after that year and sets a renewal cap of 120% of area Fair Market Rents.

DEMANDS: Tenants all over the country want the following:

1. Assure outlay funding for project-based Section 8 contract renewals and eliminate restrictions which disallow renewals based on a comparison with Fair Market Rent;
2. Eliminate language which lifts tenant protections in HUD-owned properties and those with HUD-held mortgages;
3. Eliminate language which limits project-based Section 8 renewals to one year and allows or requires conversion of Section 8 into vouchers at contract expiration;

Property Disposition

The Senate Bill allows HUD to manage and/or dispose of HUD-held Mortgages and HUD-Owned Properties (properties that have been taken over by HUD from owners who violated HUD regulations) without regard to existing laws or tenant protections.

DEMAND:

1. Preserve funding for the Property Disposition Program. The Senate version of the bill includes $261 million for the Property Disposition Program.

Mark to Market Demonstration

The Bill creates a pilot demonstration program for HUD to test a variety of approaches for dealing with expiring project-based Section 8 contracts. It will not begin until October 1, 1996. Positive elements of the proposal are:

1. Only 30,000 units are affected;
2. Only properties where rents are above 110% of area Fair Market Rents are affected;
3. Requires resident consent to substitute vouchers;
4. Criteria include various types of properties (e.g. occupancy profiles with a mixture of tenant incomes, different financial and physical conditions of buildings, etc.);
5. The demonstration program has identifiable goals including maintaining developments in decent condition, protecting tenants and surrounding neighborhoods, etc.;
6. On-going reporting and evaluation to Congress;

SHORTCOMINGS INCLUDE:

1. No guarantee the same number of very low/low income households will be served;
2. No assurance that non-performing owners will be terminated;
3. No requirement that HUD actions to deregulate restrictions be evaluated under public purpose goals (e.g. nondiscrimination against voucher holders);
4. Weak resident and community participation requirements.

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MEMORANDUM

To: John Gauthier
Staff, House Subcommittee on Appropriations
for VA, HUD, and Independent Agencies

From: Michael Kane
Executive Director, NAHT

Date: July 8, 1995

RE: NAHT Suggestions for Cost-Savings in HUD's Multi-Family Housing Preservation Program

As a follow-up to our letter dated May 23, 1995, this memorandum outlines several measures for reform and cost-savings in HUD's Housing Preservation programs which would prevent displacement of existing tenants and preserve affordable housing at the least possible cost to the federal government. These ideas have been previously suggested by NAHT in our memoranda dated February 24 and May 23, 1995 and, regarding the Capital Grant approach, by the National Housing Trust, most recently on June 14, 1995.

As you know, the National Alliance of HUD Tenants (NAHT) is a coalition of 128 tenant and associate member groups in HUD-subsidized, multi-family housing. Founded in 1992, NAHT is the first and only national voice of tenants living in the privately-owned, HUD-assisted multifamily housing stock affected by HUD's Preservation programs. We appreciate your participation in our Congressional Forum on May 23 and your willingness to consider NAHT's proposals for Title VI reform.

NAHT member groups have taken the lead in criticizing costly aspects of the Title II/VI Preservation programs, both in its original legislative design and in HUD's implementation of it. NAHT has also been in the forefront promoting cost-saving reform alternatives for several years. Tenants have the most to gain by making scarce funds meet real preservation needs, and the most to lose if the program is defunded or abolished in a misguided effort to correct program abuses and/or achieve short-term budget savings. Repeal or defunding would wreak havoc on thousands of low-income families and elderly people who would be displaced from their homes; would cost more in the long run through costly alternative public assistance and nursing home programs; and would stop resident homeownership "buy-outs" currently in process dead in their tracks.

Tenants United to Save Our Homes

NAHT is prepared to work in earnest with the Congress to realize cost-savings reform in Title VI this year. As a first step, however, Congress must preserve some funds in the FY 96 budget for Housing Preservation, and to work with NAHT and others to achieve cost-savings and Title VI reform through the authorization process.

Three strategies to preserve housing at the least cost. Generally, there are three types of cost-savings measures which NAHT has supported: 1) less costly methods to finance Preservation, notably by substituting direct Capital Grants or Loans for expensive new debt financed by Section 8 contracts; 2) reforms to HUD's Capital Needs and Appraisal processes to maximize funds spent on repairs and preservation, within the basic "Grand Compromise" enacted by Congress; 3) restricting windfall profits to the owners through limitations on government-defined "equity" value.

There is a growing Congressional, industry, and advocate consensus around the Capital Grant approach, which NAHT supports with some important caveats (see below). Billions of dollars in long-term budget authority can be saved in a reformed Title VI program utilizing some form of Capital Grant alone. The Capital Grant approach, especially for sales to resident groups and nonprofits, was cited favorably in the Congressional rescission resolution and seems likely to be enacted if funds for Preservation are preserved in the FY 96 budget.

NAHT also has proposed several cost-savings measures involving reforms to HUD's Capital Needs Assessment and appraisal reviews in the Preservation program. Billions more could be saved by some or all of these measures, which are described below. Most of these are compatible with the Capital Grant reform and could be "piggy-backed" onto it—a "Capital Grant Plus" package. These reforms would also benefit residents, communities and the housing stock by ensuring that maximum resources are devoted to repairs, and by limiting displacement of moderate income tenants when buildings are sold or refinanced.

Efforts to limit the "corporate welfare" aspects of the Title VI program by restricting owner windfalls can be expected to engender strong opposition from industry groups. However, NAHT estimates that as much as $15-20 billion could be saved by this approach, from the current IG projection of $37 billion total program costs over 15 years. NAHT believes that budget-conscious members of Congress have the power to change the terms of the windfall profits debate. The unexpectedly high cost of preservation to date, and the imbalance between windfall proftis vs. repairs/tenant protections seen in many cases, has created a growing budget crisis which deserves drastic measures—but not at the expense of the affordable housing stock or current residents. The waste is in "corporate welfare" to a tiny few. (Attached is NAHT's February 23 memorandum providing more information on our proposal to restrict windfall profits.)

NAHT Proposals to Save Funds through Reform of HUD's Title VI Preservation Program

Reform Title VI through adoption of a Capital Grant/Loan program. Generally, paying for capital costs (equity take-out and/or repair needs) by a one-time Grant or a phased Capital Loan will save money, all things being equal, in comparison to long-term debt financed by Section 8. Savings are achieved by the elimination of cumulative interest payments on loan principal, which in the current Preservation Program show up, under budget counting rules, as massive front-end commitments of Section 8 payments for long-term debt service.

HUD's Inspector General first proposed the Capital Grant alternative to save funds in the Preservation program in the IG's 1993 Multi-Region HUD Audit of the Title II program. NAHT was the first organization outside of government to support this approach, starting at HUD-sponsored forum in December 1993. This year, a growing consensus has emerged among industry, nonprofit advocates, and key Congressional staff for some kind of Capital Grant/Loan reform to the Title VI program. Several studies have now confirmed the IG's view that this approach can preserve housing at substantially less cost than the current Preservation program.

The Capital Grant version proposed by the National Housing Trust (NHT), a nonprofit advocacy group, comes close to meeting NAHT's goals of no tenant displacement and permanent preservation of affordable units. The NHT proposal would buy 50 years of preservation for the cost of a 5-year Section 8 contract in most areas, requiring equal or lower appropriations than current law (for 5 years only), and at a lower cost than providing vouchers for residents who live in these buildings (HUD's current proposal). In contrast, the current program would require continued commitments of 5-year Section 8 at a high contract rent level to cover debt service on a HUD-insured loan for the duration of the mortgage (i.e., 40 years). In a similar analysis, the IG estimated a deferred Capital Grant program could preserve buildings for about <u>one-fourth</u> the cost of the current Title VI program over a 40 year period.

However, NAHT recommends amending the NHT proposal to provide for limited commitments of Section 8 funds to ensure continued affordability for very low income (less than 50% of the PMSA median income) households; since Section 8 contract rents and the number of Section 8 units would be substantially lower than in the current Preservation program, NAHT's preservation goals could be achieved with minimal Section 8 funds. Similarly, NAHT recommends an amendment to allow HUD to make exceptions for high-cost areas to prevent tenant displacement and preserve mixed income communities.

Promote sales to resident and nonprofits: Resident and community ownership is not only good social policy; it helps save HUD money at the "back-end", when original mortgages expire, by limiting the need for yet another round of subsidy outlays to encourage owners to preserve the housing (or indirect costs if tenants are displaced at mortgage termination). Resident, nonprofit, and/or public agency owners are also less likely to speculate on housing stock and displace residents.

This is another reason why the Title VI Preservation program should be reformed, not repealed. The encouragement of sales to resident/nonprofit groups was one of the most attractive features of Title VI when it was passed in 1990. Several NAHT member groups have successfully bought their developments under Title VI or its predecessor program, Title II. Many other tenant groups are "in the pipeline" now, having donated years of volunteer time by low income tenants and raised the hopes of thousands of the poor that at last they might own a piece of America.

It is now evident that only about 25-33% of the eligible properties nationally are being offered for sale, as opposed to refinanced. The Capital Grant/Loan proposal by the National Housing Trust provides for a Capital Grant for sales, and a Capital Loan for refinancings. In addition to the Capital Grant vs. Loan distinction, Congress should consider reducing benefits (such as 241(f) mortgage insurance) to owners who "stay in" as opposed to sell to promote this objective. Given the long-term cost savings aspects of public sector sales, Congress should consider a subsidy premium. For example, other incentives could be offered through tax forgiveness and/or higher sales value for sales (as the "highest and best use" appraisal standard does now). The industry could be expected to support exemptions for higher value.

Reform Capital Needs Assessments. Currently, HUD's Capital Needs Assessment (an inspection that is done to see what work needs to be done) requirement does not take into account all of the problems tenants find in many buildings (toxics, termites, etc.). In many cases, HUD's repair standards (for example, kitchen cabinets and appliance replacement) are outdated and seriously shortchange repair needs. We need to make sure that all of these repair needs are identified.

In addition, HUD has allowed owners to "take out" equity value based on "highest and best use" market rate standards, including luxury market repair assumptions, but does not require owners to make this level of repairs as a condition of receiving refinancing subsidies from HUD. HUD should either lower equity valuations to reflect a lower standard of repairs if owners refinance, or require a higher level of repairs; owners should not be able to have it both ways. This would lower the market value of the property, saving HUD money, and ensuring that HUD funds are used maximally for needed repairs, as opposed to paying for additional windfall profits for owners. HUD should also require completion of repairs <u>before</u> rent increases or subsidy benefits are allowed in the case of refinancing, to ensure that required repairs are actually performed.

Reform Appraisal Standards. As HUD's Inspector General has noted, HUD's administration of the Preservation program has often over-valued properties, costing HUD more funds through taxpayer windfalls and displacing tenants, who pay higher ceiling rents set in faulty HUD-approved appraisals. Congress should take steps to enact reforms recommended by the IG in its 1993 Multi-Region HUD Audit of the Title II program, including adequate staffing and training for HUD's appraisers.

A Boston Globe report last December rightly criticized HUD for awarding owners more money than they had actually asked for in several cases under the Title II program. One simple reform would be to require that HUD choose the lesser of the owner's appraisal, or HUD's, as the approved equity value of a building.

Likewise, HUD's appraisers often do not take into account local laws that would prohibit conversion to a use other than affordable housing. Taking these laws into account would lower the "market" value of the property and save HUD money. Title VI should be revised to allow the tenants to bring in their own appraisers, and/or to require the owner to get a commitment from a bank. Bank appraisers are more accurate because the bank's money has to stand behind the appraisal.

Finally, HUD should be required to more accurately estimate the cost of conversion to market rate housing (i.e., how much it would actually cost to evict and relocate existing tenants and prepare for market-rate renters) in appraisal reviews to reduce windfall profits and save funds. One "conversion cost" model developed by the Massachusetts Housing Finance Agency, for example, projected savings of up to 15% off of pre-conversion market rate appraisal values. HUD's assumptions have typically yielded very minor savings in the 1. to 5% range. Congressional definition of this item alone could save billions of dollars in a reformed Preservation program.

Adjust appraisals to prevent "double-dipping". When "expiring use" buildings (apartment buildings built with subsidized HUD mortgage insurance by for-profit owners) were built over 20 years ago, owners typically made sizeable windfall profits through the sale of tax shelters--typically 250% gains on actual cash invested in the first few years. These tax losses of course represent an indirect subsidy paid by taxpayers. In the early 1980's, many investor/syndicators (who now appear to own most of these buildings) made a second windfall on the "resyndication" of HUD housing encouraged by the Economic Recovery and Tax Act (ERTA) of 1981, which allowed accelerated depreciation of occupied HUD housing.

Ironically, tax shelter profits were premised on the hypothetical" depreciation" or loss in value of the buildings, which were in fact typically gaining in value during these years. So the owners claimed the buildings were losing money, and received government subsidies in the form of tax shelters for their "losses"; now, owners claim that, oops, their buildings didn't really lose value, they gained value, and now they want the government to pay for this too. At the very least, Title VI appraisals should be reformed to deduct previously realized depreciation from current market values to prevent this "double-dipping" (as recommended internally by some HUD staff.) This reform could save billions over the life of a reformed Preservation program.

Don't reward bad owners. HUD claims that prepayment is an absolute right regardless of the owner's history. In some cases, HUD has approved refinancing plans to owners who had been subject to HUD audit findings and referred to the Justice Department for enforcement action under HUD's "equity skimming" program. Congress could amend the program to prevent owners that have failed to maintain their properties, received negative management evaluations, participated in equity skimming and otherwise engaged in practices that violate HUD regulations from prepaying, and possibly from receiving subsidies for refinancing. Congress and HUD should encourage sales to residents or nonprofit groups in these situations.

Provide resources and enlist tenants as partners to help HUD administer Title VI. As noted by the Inspector General, HUD's current staff are woefully ill-prepared to administer adequately a program as complex as Title VI. To make a reformed program work, NAHT proposes that HUD charge owners a "use fee" to cover the costs of administration and oversight, similar to user fees charged by private or state lending institutions. These fees could be used to fund and train HUD enforcement staff, or to fund "contracted" HUD employees, as provided by Congress in its 1994 amendment to HUD's Property Disposition and Foreclosure program.

In the spirit of the Administration's "Reinvention Blueprint" and Congressional interest in "privatization" and devolution of HUD functions, a user-enforcement fee could similarly be contracted by HUD to private nonprofit organizations, resident associations and/or state or local government entities for enforcement services. Consortiums of resident associations may well prove to be the most cost-effective enforcers or housing quality and management standards, since residents have the most direct stake in quality delivery of HUD's housing programs.

With miniscule private resources, NAHT and its affiliated tenant coalitions across the country have already begun to implement a "Tenants Eyes and Ears" program, tapping into the vast reservoir of volunteer talent from the people with the biggest stake and the greatest knowledge of what goes on in HUD housing: the residents. Organized tenant associations across the nation have learned how to identify problems--ranging from repair and management needs to evidence of equity skimming--and to bring them to the attention of the appropriate officials at HUD for action and enforcement. These unpaid, volunteer efforts have enabled HUD to do its job better, improved housing conditions, and have saved taxpayers millions through early correction of potentially costly problems.

Congress could assist this volunteer, private sector effort by enacting NAHT's recommendations to allow rent withholding and "repair and deduct" rights by individual tenants for documented violations of HUD standards, mandating a matching withdrawal of HUD's share of Section 8 rents into a mutually selected escrow account. Such a measure would empower individual "consumers" of HUD housing to leverage needed improvements through the exercise of direct market purchasing power. NAHT succeeded in getting HUD and Congressional support for similar measures in legislation affecting Section 8 contract renewals in 1994 (bill passed the House floor and Senate Subcommittee, but died in the Senate). Congress could revisit the concept of Tenants as Partners with HUD in Enforcement as part of an overall Title VI reform package this year.

Provide regulated vs. unrestricted market values: Limit windfall profits to the owners. In principle, Congress could determine what a fair rate of return should be for subsidized housing owners, and define this through Title VI reform legislation. The current standard of unrestricted market value unfairly rewards owners, displaces low income tenants and fails to preserve the stock. One alternative method would be to allow owners to realize gains on the actual equity they invested in the properties, or (easier to measure) the 10% equity required as a Builder/Sponsor Profit and Risk Allowance when the properties were built. Formulas adjusting this forward for inflation and perhaps adjusting for tax shelter losses and/or subsequent refinancings could be devised. NAHT tenant groups suggested this approach in the legislative debates on Title VI in 1990; Congressman Joe Kennedy and several others raised this idea in Committee, but were unable to muster sufficient support.

At the time, Congressional experts concurred with our estimate that this alternative formula would yield between $9 and 16 billion in savings from an estimated program cost of $25-30 billion. Updating for the IG's estimate of $37 billion over 15 years, we believe this approach alone could yield $15-20 billion in savings over a comparable time. The industry would still make a healthy (though lower) windfall profit thorough this "regulated market" value approach, sufficient to defend against court challenges re: "unjustified takings". Regulating market values in this manner would have the additional benefit of limiting the problem of "moderate income flight" which occurs when unrestricted market values are used in Title II/VI deals (or which would occur if owners prepayed and raised rents to market levels), since the rent established by HUD's appraisals acts as a ceiling for moderate income tenants.

It was the taxpayers, not the owners, who have built up most of the "equity" in HUD housing through generous subsidies over the years. Why shouldn't Congress be able to redefine and recapture the taxpayers' "equity" investment, in order to achieve important public purposes and save money?

Eliminate Title VI Pre-emption of Local Rent Control: Currently, Title VI specifically prohibits rent control that targets section 236 and 221(d)(3) developments. Legislation to eliminate the Title VI pre-emption of local rent control will reduce the value of the properties in cities which adopt local controls targetting these buildings, thus dramatically lowering building appraisals and preservation costs to the federal government. Such local measures would also reduce "moderate income flight" (an unintended consequence of HUD's current Preservation programs), and help tenants in the event that owners are allowed to prepay their mortgages.

While this reform would cost the government nothing, the savings could be dramatic. HUD's Inspector General in a 1993 audit in New England noted a $10.8 million difference in value at one Boston property due to failure of local HUD appraisers to take into account (among other factors) a 1988 Boston rent control ordinance: this is a $25,000 pe unit difference in value. Most recently, the application of local rent control laws in the appraisal of Tower West in New York City cut ceiling rents for tenants in half and saved millions in tax-payer financed subsidies to one owner.

If NAHT affiliates and allies were unrestrained by current preemption language in Title VI, local ordinance campaigns could flourish in several major cities (Los Angeles, San Francisco, Chicago, New York, New Jersey, as well as Boston). Even some traditional opponents of local rent controls may support limited measures which protect existing low and moderate income, "means tested" tenants only, in existing subsidized housing.

Even if the federal government does not have the chutzpah to impose windfall profit limitations, as suggested above, at least Congress should not tie the hands of state and local governments which might want to do so locally.

NATIONAL
HOUSING
TRUST

STATEMENT TO THE SENATE BANKING, HOUSING AND URBAN AFFAIRS COMMITTEE

SUBCOMMITTEE ON HOUSING OPPORTUNITY AND COMMUNITY DEVELOPMENT

Washington, D.C.

October 17, 1995

By

MICHAEL BODAKEN
NATIONAL HOUSING TRUST

Senator Mack, members of the Subcommittee, thank you for inviting the National Housing Trust to participate in this hearing today. My name is Michael Bodaken and I am the President of the National Housing Trust, a national nonprofit organization formed in 1986, dedicated exclusively to the preservation of affordable housing. Our board of directors includes representatives of all major interests in the preservation area, including tenant advocates, owners and managers, state housing agencies, national and regional nonprofit intermediaries, housing scholars and other housing professionals who care deeply about protecting this irreplaceable resource. The Trust was active in mediating the disparate interests of the housing community during the 1990 LIHPRHA debate and provided technical support to Hill staff on the 1992 and 1994 and proposed 1995 amendments to LIHPRHA.

The organization serves as an informational clearinghouse on program developments for the public and private sector. In addition to its public policy and program monitoring role, the Trust provides technical assistance to resident endorsed nonprofits on sale transactions. Finally, at HUD's request, in 1994 the Trust held a series of working sessions throughout the United States to simplify the program and reduce its cost to the American taxpayer.

Introduction

Today's testimony will cover five discrete areas:

I. Explain why, in the midst of this nation's affordable housing crisis, it is critical to preserve federally assisted, well located, mixed income housing. My testimony includes in a clear format the projects currently in the Preservation pipeline. For that data, please refer to the attached National Housing Trust database on active preservation projects, listed by state. Notably, there are currently over 133,000 units active in Preservation, in projects located in 50 states, the District of Columbia and the Caribbean. The program is truly national in scope (Points 1-3 below);

II. Review the relative costs of preservation and vouchers by comparing Preservation Rents for projects which are currently in process to the local Section 8 Fair Market Rents for the community in which the project is located and the relative cost of the capital grant program against vouchers (Point 4);

III. Explain why vouchers do not provide suitable replacement housing for displaced residents in all housing markets (Point 5)

IV. Explain why the Capital Grant proposal is the most cost effective means to preserve this mixed income housing stock which is serving residents of all incomes in urban, suburban and rural areas alike (Point 6);

V. Observe that the Abrupt Elimination or Interruption of the Multifamily Preservation Program Will Most Profoundly Impact Nonprofit and Resident Council purchasers Who Have Spent Thousands of Dollars and Hours to Preserve Their Community Resource (Point 7).

1. Preserving the Stock of Federally Assisted Housing Is Crucial

The nation's market supply of affordable housing does not currently meet the demand for that product. Our nation has experienced a 43% decline in the number of affordable rental units over the past two decades and, according to the American Housing Survey, the number of low income renters seeking affordable housing exceeded the number of affordable homes by 4.7 million, the highest number ever. [1] This housing is increasingly becoming an endangered species. According to the Joint Center for Housing Studies at Harvard University, the national goal of decent and affordable housing for all Americans remains out of reach because poverty persists and the nation is losing low cost rental units from the conventional housing inventory. The low cost housing stock declined by 130,000 units annually between 1985-1991.

As markets tighten, voucher holders will be increasingly at risk. A recent survey by the National Real Estate Index reported that, of 34 major metropolitan markets nationwide, all 34 were experiencing reduced vacancies. The index predicted national vacancy rates below 5% by 1999. Thus, as these vouchers expire, the government will pay more to renew the voucher than it would pay to preserve the stock.

There are but two ways to resolve this dilemma: 1) dramatically increase tenant purchasing power, or 2) the cost of preserving or developing housing can be reduced, thereby reducing rents.

The voucher/certificate programs essentially address the income side by providing additional income to people to pay the cost of housing that exists in the private market. There are clear advantages to this program: it is relatively easy to administer, and provides more freedom of choice.

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[1] See "In Short Supply-The Growing Affordable Housing Gap," Center on Budget and Policy Priorities, July, 1995.

The chief disadvantage of a voucher/certificate program is cost. Today, HUD provides approximately 1.5 million vouchers and certificates to those eligible for the program. The waiting lists are 2-3 years long in cities of all sizes and entirely closed in others. The National Housing Task Force estimated the cost of an income support program for only half of the households earning less than 50% of median to be $17 billion annually in 1990. Due to inflation and increased eligibility, that number is at least $20 billion today!

Another disadvantage of a "voucher solution" to all of HUD's assisted housing stock is that it doesn't work very well for housing that is decent and affordable. The Administration and Congress have properly been concerned with owners who receive taxpayer subsidies, yet permit the housing to become havens of crime. However, that is hardly characteristic of the 133,000 units in the preservation pipeline. This housing stock is the best located, most economically integrated housing in the federally assisted inventory. It reflects the need for mixed income communities that all of us, including HUD, agree need to be promoted across the nation.

The real choice to be made is the future investment we make to sustain the supply of decent, affordable housing. If we are not going to supplement incomes to the extent necessary to permit the private housing market to meet our nation's housing needs for every American, then an element of our national housing policy must be well-designed and implemented programs to preserve the *supply* of affordable housing. Assuming we determine that the housing is worth preserving, the questions revolve around the cost and design of programs intended to save the stock.

Today, my testimony will focus on the preservation of well built stock developed by the private sector in good locations over 25 years ago. The advantage of a preservation approach, if the programs are properly designed, is that the investment can create a stock of permanently affordable housing.

2. Background on Preservation

The Preservation program is designed to preserve mixed income properties that received a shallow interest subsidy from the federal government 25 years ago. Owners had a right to "prepay" their mortgages after 20 years, and terminate affordability restrictions. Approximately 4,000 properties were built during the late 1960's and 1970's, as the federal government departed from the public housing model and enlisted the private real estate sector in the provision of affordable housing. HUD permitted the developers to prepay the mortgage balance after 20 years. Prepayment terminates the federal affordability restrictions.

As properties reached their 20th anniversaries during the mid-1980's, a number of owners exercised their right to prepay. Real estate inflation during the 1970s and 1980s sharply increased the value of many of these properties. By either selling them or prepaying the HUD mortgage, owners could realize a substantial profit. Indeed, some projects were converted to market rate rental housing, others to condominiums, and in some instances, the housing was torn down to make way for commercial development. Hundreds of residents of these properties were forced to leave their homes.

The growing realization that hundreds of thousands of low and moderate income residents could lose their homes due to this 20 year time bomb spurred Congress to act.

First, temporarily, and later, permanently, Congress made preserving this mixed income housing a national priority. With the enactment of Preservation, Congress acted to preserve over 400,000 prepayment eligible units of affordable housing, averting massive displacement of low and moderate income people and loss of housing stock. The program provides purchasing advantages to residents, nonprofits and state and local governments. LIHPRHA was adopted in a *bi-partisan* manner because everyone, Republican and Democrats alike, agreed that this housing stock should be preserved.

Not all of the "eligible" Preservation properties are participating in the program. Approximately 40% of the eligible properties, almost 150,000 units, are currently participating. [2]

3. The Present Status of Preservation

This hearing occurs at a particularly auspicious time. For some time, it appeared that Preservation activity was nascent. There were those who stated that the program was "limited to a handful of states." Over the past year, data gathered by the National Housing Trust demonstrates the truly national scope of the program.

The following data summarizes activity as of July, 1995:

- Some form of activity has been taken on <u>1,186</u> Preservation properties;

- **The 1,186 Preservation Notices of Intent filed by owners involve projects in 50 states, the Caribbean, and the District of Columbia.** The program is national in scope. Over 130,000 families and elderly

[2] <u>See</u> National Housing Trust data of active LIHPRHA projects and latest figures from HUD which estimate some 90,000 "early filers", i.e., those substantially down the pipeline, some 50,000 "later filers" and a total universe of 370,000 units.

households are residing in properties where an owner has decided to participate in the Preservation program.

• The 1,186 Notices of Intent break out as follows:

• 351 Sell	(34,489 units)	(31%)
• 827 Extend	(97,758 units)	(68%)
• 8 Terminate	(783 units)	(1 %)
• TOTAL	133,030 units	100%

• In 22 states, 21 or more Notices of Intent have been filed, representing 924 projects of the 1186 total, or 78% of all property filings.

o	California	(219 Properties)	(17,660 Units)
o	Massachusetts	(59 Properties	(9,809 Units)
o	Virginia	(58 Properties)	(8,068 Units)
o	Texas	(57 Properties)	(7,689 Units)
o	Washington	(49 Properties)	(2,282 Units)
o	Oregon	(41 Properties)	(1,801 Units)
o	Wisconsin	(41 Properties)	(2,951 Units)
o	Florida	(39 Properties)	(4,955 Units)
o	Michigan	(35 Properties)	(4,741 Units)
o	Illinois	(34 Properties)	(6,642 Units)
o	Tennessee	(34 Properties)	(3,815 Units)
o	Minnesota	(30 Properties)	(3,040 Units)
o	Georgia	(26 Properties)	(2,657 Units)
o	Ohio	(26 Properties)	(3,076 Units)
o	Pennsylvania	(26 Properties)	(5,162 Units)
o	New York	(24 Properties)	(5,501 Units)
o	Connecticut	(23 Properties)	(3,743 Units)
o	South Carolina	(23 Properties)	(2,156 Units)
o	Arkansas	(21 Properties)	(1,812 Units)
o	Indiana	(21 Properties)	(2,548 Units)
o	Maryland	(21 Properties)	(4,240 Units)
o	North Carolina	(21 Properties)	(2,162 Units)

The projects range in size from 9 to 550 units. There are dozens of other "transition rule" properties, i.e., projects eligible for processing under the predecessor statute, Title II of the 1987 Act or Preservation at the owner's election. The Preservation program is truly operating throughout the nation.

Preservation, once delayed by HUD's failure to timely issue regulations or conduct timely appraisals, is now operating full speed throughout the United States. It is a cruel irony that HUD intends to eviscerate the program just as it is making a real difference.

4. It Costs Less to Preserve this Housing Than to "Voucher it Out"

HUD would restore the owner's right to prepay and provide vouchers to residents when prepayment occurs. The proposal assumes that providing vouchers to residents is somehow less expensive than preserving the stock. This is not true in most cases. In those cases where it is true, residents will be displaced.

The Trust has reviewed data on 146 properties in 21 different states comprising 14,700 apartments whose values have been reconciled through the Preservation appraisal process. **This data demonstrates that the median Preservation Rent is 10% less expensive than the median Section 8 FMR in the communities where the developments are located.**

In approximately 77% of the apartments, projected Preservation Rents are <u>less</u> expensive than the local FMR. In those cases, the Preservation Rents, on an annualized budget basis, are less expensive than the local FMR. Thus, the federal government will have to budget more to house this family with a voucher.

In approximately 23% of the apartments, Preservation Rents are <u>more</u> expensive than the local FMR. If, as the HUD suggests, prepayment is permitted *without a preservation alternative,* the tenants in these properties will be displaced because a voucher will not enable the resident to stay in his/her home at an affordable rent.

The Trust's data, though preliminary, is corroborated by national averages of preserving federally assisted housing vis-a-vis the cost of vouchers. **For example, the outlays of project based subsidies average approximately $3600/unit while the average voucher cost for this stock has been approximated by HUD to be over $7,000/unit a 94% increase!.[3]**

Finally, in the event of prepayment, <u>the median rent increase</u> to tenants residing in properties where we are assisting a resident endorsed nonprofit purchaser is <u>46%</u>.

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[3] HUD has provided the HUD-VA and Independent Appropriations Subcommittee staff estimates on utilization of $624 million in budget authority assuming a voucher cost of approximately $7000/unit!

The information strongly suggests that two likely outcomes, neither of which are desirable, result from dramatic cutbacks of Preservation: a) the federal government will pay more to house the current residents of many of these properties (i.e., where the Preservation Rent is less than the local FMR) or b) the residents will be displaced (i.e., where the Preservation Rent is higher than the FMR).

In the face of these statistics, some blithely argue that there won't be increased costs because owners won't prepay the HUD financed mortgage. Therefore, the argument goes, few vouchers would be required for residents of these Preservation eligible properties.

The facts are otherwise. Experts in today's panel will explain the grim reality that awaits if the prepayment option is restored without a preservation option. *HUD itself assumes that 70% of the active pipeline properties will prepay.* In Illinois, for example, two owners prepaid prior to the enactment of Preservation and achieved market rents in the same market area. Rents doubled and residents were displaced. This is the same neighborhood where 1,000 units are currently processing under the Preservation law. Because many of these projects are now nearing the quarter century mark, the amount of first mortgage debt is significantly reduced. With the passage of time, as mortgage payments are increasingly applied to principal with no offsetting depreciation, owners increasingly experience the phenomenon of "phantom income" (taxable income that exceeds the property's cash flow). The traditional solution is to refinance, or prepay, the mortgage. The economic reality is that prepayment is as, or more, likely today than in 1990 when Preservation was enacted.[4]

5. Vouchers Will Not Necessarily Protect Preservation Residents

The substitution of portable vouchers *theoretically* means that tenants will rent in the private market rather than be assigned to public or federally assisted housing. Vouchers do give some tenants better and more choices in *some* housing markets.

It does not follow, however, that vouchers or certificates are adequate to provide suitable replacement housing for displaced residents of preservation properties. This is not the case for several reasons. First, as noted, the voucher may not provide enough subsidy to permit the family to stay in place. Second, in many urban markets, it is difficult for residents to locate and secure 3 or 4

[4] Indeed, the real estate industry has recently sponsored least two well attended seminars for lenders, owners, and tax advisors to discuss how to access prepayment financing if LIHPRHA or some other preservation option is not maintained.

bedroom apartments with vouchers. Also, displaced seniors will have great difficulty accessing units with meals and support systems. Further, vouchers appear not to work as well for families facing discriminatory barriers, such as minorities and handicapped individuals. Finally, vouchers provide absolutely no protection in the circumstance where the owner seeks to convert the housing to condominiums or where the owner, seeking to achieve a market definition for his/her property will not choose to participate in a HUD subsidized program.

Much has been said about vouchers providing residents choice. In preservation transactions, it is my absolute belief that residents want to stay in their homes. In the preservation transactions currently being conducted by the National Housing Trust and the Preservation Working Group, which provides assistance to over 100 projects for sale in the United States, *the residents have endorsed, in writing, the purchase of the housing. These residents want to stay, not flee.* This argues for preserving the housing now as a unique community resource to help serve mixed income, racially diverse populations.

6. The Capital Grant Approach Is the Best Vehicle for Preserving These Mixed Income Developments Which Serve as a Unique Community Resource.

The need to preserve this housing does not mean that it must be preserved at an enormous cost to the federal government with funding based upon project based Section 8 financing.

Under any circumstance, the capital grant proposal adopted by the Senate in its recent passage of the VA-HUD and Independent Agencies Appropriations Bill (H.R. 2099) recognizes that a principal benefit enjoyed by these properties is their mixed income nature and the need to serve the current residents in that community.

As in 1990, the Senate, in a bi-partisan manner, has agreed on the goal: preserving this housing stock. The concept is straightforward. This proposal would substitute a direct capital grant for the insured second mortgage financing for equity take out, acquisition and rehabilitation. It would require no new Section 8 assistance to finance the HUD insured loan.

This proposal would maintain the current rent schedule, i.e., residents paying more than 30% of their incomes would not receive rent decreases; residents paying less than 30% of their income would not pay rent increases. Under capital grant, as adopted by the Senate, the purchaser can create an operating reserve and receive excess 236 income on the property to mitigate against any future rent increases on very low income residents.

This approach would simplify the program administratively as well as dramatically reduce long term costs by eliminating the repayment of the 241(f) loan over a 40 year term. [5] *Notably, this approach would maintain the economic mix of the projects.* Finally, by preventing rent increases, it would serve as an anti-displacement measure.

The chief advantage of this approach is that the stock would be preserved by the year 2000 and the mixed income nature of the residency could remain intact. A number of observers have expressed concern that the property will not remain affordable over time. In response, I need to point out that the capital grant included in the VA-HUD and Independent Agencies Appropriations measure includes the following safeguards to assure continued affordability:

- By freezing the current rent structure, much of which is either below 30% of income or is currently provided ongoing subsidy by LMSA, the property enters the market as affordable. On that we can all agree.

- In the future, the program provides that the reserve for the replacements goes to the purchaser, not the owner. The owner also can take advantage of the rehabilitation grant to create operating efficiencies which is the single biggest cause for future rent increases.

- In the case of nonprofit purchases, the owner is provided an operating reserve and excess Section 236 income returns to the property to mitigate against future rent increases for presently unassisted residents.[6]

- Because the owner is not relying on property based, deep Section 8 subsidy, the nonprofit or for profit owner is forced to achieve operating efficiencies. This mitigates against future rent increases .

Finally, the Capital Grant is less expensive than the voucher alternative.. The Trust is aware that HUD has preliminarily taken the view that vouchers are less expensive than capital grants. That view is only sustainable in the very short term. Attached to my testimony is data provided by ReCap Advisors, which demonstrates that estimates the cost of restoring the prepayment right without a

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[5] A variant of this approach would be to pay off the first mortgage as well as the preservation equity, rehab, and transaction costs. The HUD Inspector General recommends this approach in its April 20, 1994 HUD Inspector General Audit, Review of Multifamily Preservation Programs. While very cost effective compared to Section 8 financing, this alternative requires more additional up front budget authority to preserve LIHPRHA active properties.

[6] The proposal also allows the purchaser to treat the grant in the form of a loan to seek tax credits to supplement the need for non-preservation resources to fund the transaction. Additionally, the legislation should repeal the present barrier between HOME funds and preservation funds which makes it impossible for a nonprofit purchaser to mix HOME funds with preservation resources to preserve these properties.

voucher alternative. The total outlays required is nearly $2 billion for the next seven years. After that the costs continue to go up! The total budget authority during the next 7 years is nearly $3.2 billion (without resorting to budget gimmicks). By contrast, those who have costed out capital grant agree that the average cost of preserving the 100,000 units of stock is approximately $2 billion (without the outlays associated with the new voucher created by the full bore restoration of the prepayment right). And, of course, in the meantime the nation has lost over 100,000 units of decent, well maintained, well located affordable housing stock which sere as the backbone of many of our communities.

It is absolutely contrary to the drive to a balanced budget to <u>create a new entitlement</u>: *new vouchers for tens of thousands of families who are presently unassisted. Once this rental assistance is provided, will it be removed?* What residents fear and that Congress will come to regret, is that each year there will be intense pressure to renew the vouchers for existing households and, as now, there will uncertainty every September until Congress adopts appropriations for the following year.

7. Any Proposal to Modify Preservation Must Take Into Account the Existing Pipeline and the Current Participants in the Program, Particularly Nonprofit and Resident Endorsed Purchasers. One Means of Doing So Exists in the Present Law.

Any particular proposal to modify the present Preservation law must be carefully considered. Equally important, it is important that there be a <u>transition</u> until a capital grant solution can be implemented. *As I mentioned earlier, the vast majority of the likely participants in the program are already active in the pipeline. It is essential that, pending development of the capital grant or other proposals, a viable preservation option be maintained. Otherwise, due to the frustration of many owners, particularly those owners who are seeking to sell their properties, if there is a gap, massive prepayments will occur as the private sector seek to maximize its return.*

Much has been said about the "queue," , i.e., the unfunded, but approved Plans of Action, The Trust has scrutinized HUD's data and determined that outside the "queue," fully 50% of the properties which could close in FY'96 are for sales to priority purchasers. 59% of this number are sales properties where an owner must first offer the property to a resident endorsed nonprofit or resident council.

Nonprofit purchasers have invested substantial investments of work and money into making these units permanently affordable. The Trust, for example, represents 7 nonprofit and resident groups who intend to purchase these properties. The Trust and our clients have invested literally thousands of hours in our efforts to purchase these properties. The abrupt elimination of the program will have truly profound and harmful impacts on our efforts to empower residents and save communities.

In each case of our representation, the nonprofit has been endorsed, in writing, by the residents at least twice: once to apply for a grant to complete the purchase and once to approve the bona fide offer to the owner. In each case at least one third of the board purchasing the property will be comprised of residents. This is **prima facie** evidence of the residents' intent to not only stay but to participate in the ownership and management of their homes. No such evidence has been, nor could be, offered that these residents could rather have a voucher. **It seems manifestly unjust to now eviscerate the preservation program created to preserve these properties.**

In the event that Congress decides to modify the capital grant program embodied in H.R. 2099, there is a simple means to protect priority purchasers during the interim in the present law:

Section 220(d)(3)(B) of the 1990 Act authorizes a capital grant for priority purchasers to cover acquisition, rehabilitation and other expenses in an amount equal to the Section 8 FMR over 10 years (or for a longer period, if necessary, to cover the costs identified in the law elsewhere). In that sense, capital grant is only "new" for stay-in owners and other qualified purchasers. *The present regulations and law thus provide a transition to capital grant for sales to resident endorsed and other priority purchasers.*

Conclusion

We stand on the threshold of housing history. It is tempting to believe that simple solutions can be quickly crafted to resolve the preservation dilemma in the context of rigorous budget caps and increasingly scarce resources. The truth is that these policy choices are thorny and do not lend themselves to simple examination.

At the same time, now is a time for us to "re-think" how we preserve good housing stock in decent neighborhoods, housing that serves as a unique resource to communities. The irreplaceable stock in the Preservation pipeline can be preserved, at an affordable cost to the American taxpayer.

STATUS OF TITLE VI PROJECTS: STATES RANKED BY LEVEL OF ACTIVITY

State	Number of Units	Number of Projects	Filed Notice to Extend	Filed Notice to Sell	Filed Notice to Terminate	Active Title VI Projects Not Yet Funded as of 7/5/95*	Total Title VI Units with Notices of Intent Filed
California	44,815	501	152	67	0	219	17,660
Massachusetts	27,237	156	47	12	0	59	9,809
Virginia	15,708	114	46	12	0	58	8,068
Texas	26,738	212	37	20	0	57	7,689
Washington	7,868	134	16	33	0	49	2,282
Oregon	4,931	117	25	16	0	41	1,801
Wisconsin	7,861	103	29	12	0	41	2,951
Florida	13,319	105	22	15	2	39	4,955
Michigan	21,221	136	27	8	0	35	4,741
Illinois	23,564	131	25	9	0	34	6,642
Tennessee	11,828	104	20	13	1	34	3,815
Minnesota	7,172	71	21	8	1	30	3,040
Georgia	12,004	113	23	2	1	26	2,657
Ohio	24,342	247	24	2	0	26	3,076
Pennsylvania	19,386	119	21	5	0	26	5,162
New York	60,590	236	22	2	0	24	5,501
Connecticut	13,977	105	17	6	0	23	3,743
South Carolina	6,113	61	17	6	0	23	2,156
Arkansas	4,379	55	16	6	0	22	1,812
Indiana	13,534	90	15	6	0	21	2,548
Maryland	16,872	101	14	6	1	21	4,240
North Carolina	7,340	76	16	5	0	21	2,162
Louisiana	7,927	53	12	7	0	19	2,815
Colorado	6,870	80	11	7	0	18	1,932
Arizona	3,289	36	14	3	0	17	1,626
Kentucky	6,010	77	8	7	2	17	1,710
New Jersey	9,280	92	12	3	0	15	1,683
Rhode Island	4,860	40	12	3	0	15	2,040
Iowa	3,572	37	10	3	0	13	1,330

STATUS OF TITLE VI PROJECTS: STATES RANKED BY LEVEL OF ACTIVITY

State	Number of Units	Number of Projects	Filed Notice to Extend	Filed Notice to Sell	Filed Notice to Terminate	Active Title VI Projects Not Yet Funded as of 7/5/95*	Total Title VI Units with Notices of Intent Filed
Missouri	9,145	85	6	7	0	13	1,525
Idaho	1,143	27	6	6	0	12	544
Montana	1,352	21	10	1	0	11	690
New Mexico	3,203	32	9	2	0	11	1,626
South Dakota	2,247	58	9	1	0	10	486
Alabama	4,051	41	6	3	0	9	808
Nebraska	1,576	20	5	4	0	9	646
Utah	1,003	21	6	3	0	9	468
Kansas	1,410	19	6	1	0	7	394
Mississippi	3,382	34	7	0	0	7	656
North Dakota	412	9	4	3	0	7	382
Nevada	1,312	13	5	1	0	6	565
Caribbean	5,078	26	0	5	0	5	1,102
Hawaii	1,883	16	0	5	0	5	589
Dist. of Columbia	4,928	30	3	1	0	4	692
New Hampshire	2,024	19	4	0	0	4	600
Alaska	588	9	2	1	0	3	316
Maine	1,691	15	1	2	0	3	229
Delaware	636	5	2	0	0	2	334
Oklahoma	4,581	42	2	0	0	2	350
Vermont	884	7	1	1	0	2	220
West Virginia	274	3	1	0	0	1	150
Wyoming	509	11	1	0	0	1	12
TOTALS	485,919	4,065	827	351	8	1186	133,030

SOURCE: This listing combines information from HUD, Fannie Mae, Selected State Agencies, and preservation advocates who monitor notices, including CHPC and CCDC.

* This report does not include projects for which initial NOIs had been filed subsequent to 12/31/94.

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6/3/95

Affordable Housing Preservation
Appropriations Required if Prepayment Allowed

Summary

If owners of LIHPRHA-eligible property regain the right to prepay, roughly 75,000 incremental Section 8 vouchers will be required, at a total Federal outlay (*net* of Section 236 Interest Reduction Payment recapture) over the next seven years, of ***$2.0 billion***. Budget authority required will be $3.3 billion.

Projected Prepayments

Appropriations required are calculated on the attached schedule and its footnotes. Principal conclusions from the analysis:

1. ***At least 85% of LIHPRHA pipeline owners will prepay***. About 77% of the apartments now in the pipeline are in properties with at least $1,000,000 Preservation Equity per property. We expect that *all* of these owners will prepay as rapidly as they can arrange takeout financing. A further 15% of the portfolio has between $500,000 and $1,000,000 in Preservation Equity. We estimate that at least *half* of these owners will prepay as well.

2. ***Pipeline prepayments will occur rapidly, most within 12 months***. Even if the property is only at breakeven today, prepayment will be *viable* if an owner can raise rents as little as $50 per month, and nearly all LIHPRHA-viable properties will be able to do that almost immediately. Arranging the necessary financing should also be straightforward: a new loan need only pay off the HUD mortgage (typically about $11,000 per apartment today), which represents 50% or less of the property's estimated post-conversion value.

3. ***Other properties not in the pipeline will also prepay***. Beyond the properties with immediate conversion potential are another 15,000 apartments in the LIHPRHA pipeline, plus another 250,000 apartments, not yet proceeding under LIHPRHA, which will be prepayment-eligible. Even if these properties have little or no value today, some of their owners will elect to prepay, if only to escape HUD regulatory burdens and the uncertainty attendant upon the HUD portfolio.

   We believe that many of these properties will eventually prepay, but have eliminated them from consideration, chiefly for consistency of comparison with the cost of preserving the LIHPRHA pipeline under capital grant/loan.

Costs in 1,000,000 's

06/03/95

Affordable Housing Preservation

Net Outlays Required If Prepayment Right Restored

Prepayments (85% of pipeline)		FY 96	FY 97	FY 98	FY 99	FY 00	FY 01	FY 02	Total
Very low income	*67%* of residents	*37,967*	*9,492*	*9,491*	*0*	*0*	*0*	*0*	56,950
Low income	*22%* of residents	*12,467*	*3,117*	*3,116*	*0*	*0*	*0*	*0*	18,700
Total apartments prepaying		50,434	12,609	12,607	0	0	0	0	75,650

FY 96	Very low income	133.7	137.7	230.0	236.9	244.0	251.3	258.9	1,492.6
FY 96	Low income	9.6	9.9	10.2	10.5	10.8	11.1	11.5	73.7
FY 97	Very low income		34.4	35.5	59.2	61.0	62.8	64.7	317.7
FY 97	Low income		2.4	2.5	2.5	2.6	2.7	2.8	15.5
FY 98	Very low income			35.5	36.5	61.0	62.8	64.7	260.6
FY 98	Low income			2.4	2.5	2.5	2.6	2.7	12.8
Minus Section 236 IRP recapture		(20.6)	(25.8)	(30.9)	(30.9)	(30.9)	(30.9)	(30.9)	(201.0)
New outlays required in ...		122.7	158.7	285.1	317.3	351.1	362.6	374.4	**1,971.8**

Assumptions About Properties in the Pipeline			
575	Section 8 FMR (national median, 2-BR apt)	*40,200*	National median income, family of four
68%	Current rent as a percentage of Section 8 FMR	*30%*	of income for rent (including utilities)
391	Current budget-based rent	*100,000*	Apartments in the LIHPRHA pipeline
25	Current Personal Benefit Expense (PBE)	*85%*	of pipeline owners would prepay
8.2%	Section 8 voucher contract administrative fee	*619*	Section 236 Interest Reduction Payments per apartment
2.0	Years remaining on existing Section 8 LMSA	*66%*	of pipeline properties are Section 236

Voucher Outlays per Apartment	FY 96	FY 97	FY 98	FY 99	FY 00	FY 01	FY 02
Very low income with Section 8	3,522	3,628	3,736	3,848	3,964	4,083	4,205
Very low income without Sec 8	5,710	5,882	6,058	6,240	6,427	6,620	6,818
Low income	771	794	818	842	868	894	921

Property Resident Income Mix (before prepayment)	Very low with Sec 8	Very low w/o Sec 8	Low with Sec 8	Low w/o Sec 8	Moderate
Residents in this category	*40%*	*27%*	*0%*	22%	11%
Family income as percent of median	*11%*	*26%*	*58%*	58%	*89%*
Do they receive Section 8 vouchers?	*Yes*	*Yes*	*Yes*	*Yes*	*No*

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This schedule should be read in conjunction with the memorandum, ***Prepayment Appropriations Assumptions and Analysis***, which accompanies it and provides explanation and evidence for the assumptions presented here. Section 8 subsidy costs assume *3%* annual inflation over the seven year period.

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Costs in 1,000,000 's

06/03/95

Affordable Housing Preservation

Budget Authority Required If Prepayment Right Restored

Prepayments (85% of pipeline)		FY 96	FY 97	FY 98	FY 99	FY 00	FY 01	FY 02	Total
Very low income	*67%* of residents	*37,967*	*9,492*	*9,491*	*0*	*0*	*0*	*0*	56,950
Low income	*22%* of residents	*12,467*	*3,117*	*3,116*	*0*	*0*	*0*	*0*	18,700
Total apartments prepaying		50,434	12,609	12,607	0	0	0	0	75,650

FY 96	Very low income	181.7	187.1	312.8	322.2	331.8	341.8	352.1	2,029.5
FY 96	Low income	96.8	99.7	102.7	105.8	109.0	112.2	115.6	741.9
FY 97	Very low income		46.8	48.2	80.5	83.0	85.5	88.0	432.0
FY 97	Low income		24.2	24.9	25.7	26.5	27.2	28.1	156.6
FY 98	Very low income			48.2	49.6	83.0	85.5	88.0	354.3
FY 98	Low income			24.2	24.9	25.7	26.4	27.2	128.5
Minus Section 236 IRP recapture		(267.9)	(87.6)	(92.7)	(30.9)	(30.9)	(30.9)	(30.9)	(572.0)
Budget authority required in ...		10.6	270.3	468.3	577.8	628.0	647.7	668.1	3,270.7

Assumptions About Properties in the Pipeline			
575	Section 8 FMR (national median, 2-BR apt)	*40,200*	National median income, family of four
68%	Current rent as a percentage of Section 8 FMR	*30%*	of income for rent (including utilities)
391	Current budget-based rent	*100,000*	Apartments in the LIHPRHA pipeline
25	Current Personal Benefit Expense (PBE)	*85%*	of pipeline owners would prepay
8.2%	Section 8 voucher contract administrative fee	*619*	Section 236 Interest Reduction Payments per apartment
2.0	Years remaining on existing Section 8 LMSA	*66%*	of pipeline properties are Section 236

Voucher Budget Authority per Apartment	FY 96	FY 97	FY 98	FY 99	FY 00	FY 01	FY 02
Very low income with Section 8	4,786	4,929	5,077	5,229	5,386	5,548	5,714
Very low income without Sec 8	7,766	7,999	8,239	8,486	8,740	9,003	9,273
Low income	7,766	7,999	8,239	8,486	8,740	9,003	9,273

Property Resident Income Mix (before prepayment)	Very low with Sec 8	Very low w/o Sec 8	Low with Sec 8	Low w/o Sec 8	Moderate
Residents in this category	*40%*	*27%*	*0%*	*22%*	*11%*
Family income as percent of median	*0%*	*0%*	*0%*	0%	*89%*
Do they receive Section 8 vouchers?	*Yes*	*Yes*	*Yes*	*Yes*	*No*

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This schedule should be read in conjunction with the memorandum, ***Prepayment Appropriations Assumptions and Analysis***, which accompanies it and provides explanation and evidence for the assumptions presented here. Section 8 subsidy costs assume *3%* annual inflation over the seven year period.

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PREPAYMENT APPROPRIATIONS (BUDGET AUTHORITY AND OUTLAYS)

ASSUMPTIONS AND ANALYSIS

Summary

Best available evidence suggests that allowing owners in the LIHPRHA pipeline to prepay will cost the Federal government about ***$2.0 billion*** in incremental outlays (and ***$3.3 billion*** in budget authority) over the next seven years (FY 96 through FY 2002). This memorandum summarizes the principal assumptions involved in deriving that figure.

Assumptions and Analysis

Principal assumptions and the data sources from which they were derived:

Element	Assumption	Derivation and evidence
Current rents as a percentage of FMR	68%	Compiled from about 60,000 LIHPRHA apartments that have reconciled their appraisals with HUD.
Current PBE's	$25	Recap Advisors estimate.
Market rents on prepayment	100%	Statistical analysis has shown that LIHPRHA-viable apartments have market rents that reasonably approximate the current FMR. The Administration has recently proposed lowering the Section 8 FMR's from the 45th to the 40th percentile. Such a change, if made, would have no effect on the estimated prepayments (which derive from *true market rents*, not HUD FMR's).
Section 8 voucher rent as percentage of FMR	100%	Current policy. The Administration has recently proposed lowering the Section 8 FMR's from the 45th to the 40th percentile. If made, this change would reduce the net outlay costs of delivering Section 8 vouchers to displaced residents, but would correspondingly increase overall displacement and resident hardship.

Element	Assumption	Derivation and evidence
Section 8 administrative fee as a percent of rent	8.2%	Current policy. Section 8 vouchers are administered by public housing authorities (PHA's) who are paid a monthly administrative fee.
Apartments in pipeline	100,000	Compiled from responses to Freedom of Information Act (FOIA) requests to all HUD field offices. The actual pipeline is larger (about 150,000 apartments), but we have subtracted estimates of (a) properties that have already closed LIHPRHA recapitalizations, and (b) 'false positives': recent filings of properties with no real Preservation Equity.
Pipeline apartments that would prepay	85%	Assumes prepayment by all owners with Preservation Equity per property of $1,000,000 or more (77% of the pipeline), plus half of those between $500,000 and $1,000,000 in equity (another 15% of the pipeline). This figure is conservative because it ignores any potential prepayments from (1) pipeline owners with less than $500,000 in equity (about 8,000 apartments) or (2) owners who have yet to file LIHPRHA Notices of Intent (another 250,000 apartments).
Timing of prepayments: Within 12 months 12 to 24 months 24 to 36 months	 67% 16% 16%	Recap Advisors estimate. Owners whose equity is greater will generally prepay first. In addition, it will take the typical owner some time to arrange new financing. This timetable is thus largely a matter of assessing how quickly the owner will be able to assemble the necessary financing.
Percentage Section 8 LMSA on property now	40%	Compiled by Recap Advisors from a large representative national portfolio. Compared with the portfolio as a whole, LIHPRHA-viable properties tend to have slightly less Section 8 LMSA, because they have higher value and thus were less likely to have needed LMSA in the past. All current LMSA apartments are assumed to be occupied by very low income residents; although occupancy by low-income is possible, under Section 8 rules in force since 1981, new applicants must be very low income, and we believe that as a practical matter essentially all such apartments are indeed very low income.

Element	Assumption	Derivation and evidence
Years remaining on Section 8 LMSA	2	New LMSA contracts are five years or less; in recent years HUD has been shortening renewal terms, partly in an effort to conserve budget authority. When an LMSA Section 8 contract is in place at the property today, we have calculated only the *incremental* outlays resulting from (1) extending Section 8 to residents who qualify but are not currently receiving it, (2) increasing rents to market (which we have assumed is the Section 8 FMR), and (3) covering Section 8 costs after the current short-term LMSA contract expires.
Resident income mix: Very low income Low income Moderate/market	 67% 22% 11%	Compiled by Recap Advisors from 10,000 apartments in their LIHPRHA Plan of Action phase. These figures correspond well to overall portfolio figures which HUD has compiled in other contexts.
Incomes as percentages of area median: VLI with Section 8 now VLI without Section 8 Low income Moderate/market	 11% 26% 58% 89%	Compiled by Recap Advisors from 10,000 apartments in their LIHPRHA Plan of Action phase. These figures correspond well to overall portfolio figures which HUD has compiled in other contexts. We chose to draw a distinction among very low income residents based on whether they now have Section 8 LMSA, because analysis shows that, at 11% of area median income, a very low income resident without Section 8 could not possibly afford the apartment. Hence these residents must have higher income from some source.
Section 8 tenant share as a percentage of income	30%	As provided under current law. The Administration has proposed an increase to 35%.
Annual inflation	3%	Recap Advisors assumption based on average inflation over the last three to four years.
Section 236 IRP per apartment per year	$619	Recap Advisors assumption based on a typical Section 236 loan with original balance of $14,000 and interest at 7.0%, reduced by Interest Reduction Payments to an effective rate of 1.0% per year (3.03% debt service constant).

Element	Assumption	Derivation and evidence
Percentage of pipeline that receives Section 236	66%	About 71% of HUD's 360,000-apartment Preservation Inventory consists of Section 236 properties; however, Section 221(d)(3) properties are more likely to have Preservation Equity (they are older, have lower average mortgage balances, and their debt service is less reduced). Statistics show that, of the first 23,000 apartments in the LIHPRHA pipeline, about 66% were Section 236.

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outlays vs b.a.

Andrew

11/2 Preserv Mtg Marc Cranomiller, Elena Popp

Diff w/ MTM → tax proposal
Our ~~position~~ proposal → targeted presv to non-profits

HUD → vouchers, then preserv.
→ Preserve, then vouchers
"devils in details"

MTM
fed: $3M mortgage
+ 1-2M rental assistance

- less expensive than vouchers

LIPRHA
3 costs - 1 - equity
2 - repairs
3 - transaction costs

Restored in rescission.

624M → budget authorities
440 → outlays (assuming not redesigned)

under Senate, HUD would have to continue to fund old program

Tenants: don't have to restore it to prepay
HUD: will result in lawsuits

Preserv - HUD initially zeroed
- Mikulski amend to transfer $ from Preserv to seniors
- Where is OMB?

Testimony before the

Committee on Banking Housing and Urban Affairs
Subcommittee on Housing Opportunity and
Community Development

United States Senate

October 17, 1995

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

NICOLAS P. RETSINAS

ASSISTANT SECRETARY FOR HOUSING
FEDERAL HOUSING COMMISSIONER

STATEMENT OF

NICOLAS P. RETSINAS
ASSISTANT SECRETARY FOR HOUSING - FEDERAL HOUSING COMMISSIONER

Before the

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
SUBCOMMITTEE ON HOUSING OPPORTUNITY & COMMUNITY DEVELOPMENT
UNITED STATES SENATE

October 17, 1995

Mr. Chairman and Members of the Committee:

Thank you for inviting me here today to participate as a partner with you in our mutual efforts to improve the way we preserve affordable housing opportunities. In my brief remarks, I would like to share with you some facts and numbers which tell where we are today and what is at stake regarding the issue of preservation. Finally, I would like to suggest for your consideration some core principles to guide us in our deliberations.

Prior to assuming my position with HUD as Assistant Secretary for Housing, I co-authored an article about preservation, especially as it relates to Elderly housing. At that time, I predicted that the current legislation might not work easily or efficiently. I now know first-hand the wisdom of that earlier prophecy.

When we crafted the current preservation language -- and I say "we" because many of us in this room were involved -- we envisioned a crisis which would result in the loss of hundreds of thousands of units of affordable housing and the diplacement of thousands of residents. The existing preservation program was a noble effort to forestall that problem. Now, however, with the benefit of hindsight, we are able to see the problem more clearly and also to see the strengths and weaknesses of the program we crafted.

Thus, my comments are not meant to criticize or denigrate the important efforts of all who participated in developing the program. Rather, we can use our experience to strengthen what we do in the future in this environment of constrained resources.

BACKGROUND ON CURRENT PROGRAMS

Building on interim legislation enacted in 1987, the Congress developed an approach that practically precluded any prepayments and promised to pay virtually any price to achieve that objective. That strategy set up a procedure that restricts owners' prepayment rights or, as some have argued, closely resembled an eminent domain taking process. In any event, the procedure was complex and detailed, including multiple appraisals, with no practical limits on costs.

The existing program relies on two fundamental subsidies: increased debt, insured by the FHA fund and increased Section 8 subsidies, to support this debt. By doing this, we increased the long term liabilities of the federal government, through the FHA insurance fund, sometimes extending far beyond the Section 8 subsidy commitment. To put numbers on this, we have created 35,000 new units of Section 8 subsidy, costing approximately $230 million a year, in addition to Section 8 subsidy supplements to units already in place.

Today, 227 approved preservation Plans of Action are waiting to be funded at over $700 million in new budget authority. One could argue, Mr. Chairman, that preservation has achieved its objectives -- but at a current and future cost that we can no longer afford if indeed we ever could.

STATUS OF PRESERVATION PIPELINE

There is a certain irony in the fact that we have increased by tenfold the number of projects processed in any given year during our administration. In the four years from 1989 to 1993, we processed only 120 projects. In 1994 alone, we processed an additional 120 projects. And in 1995, we processed 266 projects, or double the 1994 level.

Approved Projects

Since the beginning of the current laws on preservation, we have approved Plans of Action for 738 projects through September 30th of this year. These projects represent just under 90,000 units, broken down as follows:

-- 511 projects, with approximately 63,000 units, were approved and funded at a cost of $1.2 billion -- but only for the first five years of preservation. This cost has to be continued for at least the full remaining term of the mortgage.

-- Another 227 projects, with 27,000 units, are in the unfunded pipeline queue. The total cost of funding these projects would be over $700 million.

Projects in Processing

There are an additional 1,100 projects with 126,500 units that are in processing. Slightly more than 800 of thesed projects have not reached the completion of their appraisal process, with the remainder awaiting plan of action approvals. If all of these projects were to be approved -- clearly, not all of them would -- the total cost to the taxpayers, based on current cost experience, would be almost $2.5 billion.

Eligible Projects Not in Processing

As for eligible projects not in processing, there are 1,855 insured projects with 188,665 units that have not initiated any filing under the preservation program. Additionally, it is believed that there are approximately 70,000 units of State Agency non-insured projects that have not filed.

BASIC PRINCIPLES OF REFORM

Mr. Chairman, notwithstanding this status report, numbers alone do not fully capture the overriding budget issue that is driving the preservation policy debate. We believe that our current efforts at preservation are too costly and cannot be sustained given today's budgetary realities. Therefore, Mr. Chairman, if the current approach is simply too costly, how do we proceed from here?

Quotes from Inspector General

Mr. Chairman, let me quote from a recent report of our Inspector General's office regarding the Multifamily Preservation Program:

> "We believe that the Preservation Program should be repealed, thereby eliminating the project owner's ability to obtain equity from the project without taking any risk. Repeal would also eliminate the need for additional project-based subsidies. **Project owners would be allowed the uncontested option of prepayment and tenants would be provided tenant-based subsidies, giving them the freedom to choose where to live.**"

Quoting from the same report dated July 14, 1995, the IG's office states:

> "HUD has an opportunity to make a clean break from policies and programs that failed in the past and to pursue new approaches to old problems that have long beset HUD's Multifamily Programs. As this study points out, there is no easy solution to the preservation problem. However, **the cornerstone for correcting the problem, both from the cost and legal aspects, must include the uncontested option for the project owner to prepay as HUD's proposed**

"New Preservation" program does. Prepayment allows the greatest flexibility for the market to establish both the rents for tenants and the value of the project for the owners."

We have learned a number of lessons from our experience in administering Preservation programs under Titles II and VI. We wish to apply the lessons gained from our experience in such a way as to protect residents from adverse consequences of our actions in this area. My principal concern as Assistant Secretary for Housing and Federal Housing Commissioner is to assure that existing residents continue to reside in affordable rental housing.

Fundamental to reforming Preservation is changing the priorities from owner compensation to resident protection. This means that, as the owners' right to prepay is restored, the residents must be protected from any threats that may arise to their continued residency.

Mr. Chairman, cognizant of the findings by HUD's Inspector General, I believe there are certain actions we can and should take to reform and improve the Preservation Program, and I would like to review with you those actions or guiding principles.

1. **Protect residents**. The first action relates to my foremost concern, Mr. Chairman, and that is resident protection. I know that you share this concern. Whatever course of action is taken, residents must come first. The protection of residents can be achieved in part by the provision of vouchers. I will elaborate on that in a few moments.

2. **Restore the right to prepay.** Secondly, if we agree that, under the current budget realities, the current approach to preservation is too costly, we must restore the right of owners to prepay their mortgages. As stated before, to do otherwise leads to an expensive and convoluted process.

ISSUES AND OPTIONS

With these principles in mind, let me suggest some issues and options for your consideration, Mr. Chairman, that would reflect these principles.

Protection of Residents

In the case of prepayments, current contracts would continue as project-based until they expire and, when they do expire, the same policies as for other contract expirations would apply.

The more difficult question, Mr. Chairman, is how to deal with those residents not now receiving Section 8 assistance who would be effected by the removal of use restrictions and increases in rents upon prepayment.

If these residents are to be protected from rent increases, the first question is where to establish the level of benefit. Should all currently unassisted residents whose incomes are at or below 80 percent of area median income be protected, or should the eligibility line be drawn at a lower level -- say, 60 percent or 50 percent of median income? Clearly, the higher the line is drawn the more costly the protections become, but also as resident incomes increase, the subsidy costs decrease.

Our information indicates that, based on the current preservation portfolio, approximately 10 percent of the residents are above 80 percent of median income -- and thus are ineligible for housing assistance. The remaining 90 percent of the residents is split roughly evenly between those residents currently receiving Section 8 assistance and those not receiving any assistance. Of those who are not now receiving assistance, a little more than one-half are very low income -- that is, those whose incomes are at 50 percent or less of area median income. That leaves a little less than one-half that are 50 to 80 percent of median income.

The next question, Mr. Chairman, is what level of protection is provided for those residents receiving vouchers whose rents after prepayment are greater than the voucher payment standard. Should those residents be assisted up to that new rent to prevent their being displaced? Should distinctions be made between types of residents if this protection were to be provided-- e.g., elderly, disabled, families -- or should all be protected?

Moreover, should there be any time limits placed on this additional form of protection? Again, these protections add cost, but the amount of the cost increase needs to be balanced against the disruption in the lives of these vulnerable people.

We are prepared to work with you, Mr. Chairman, to attempt to resolve these two basic questions:

1. **Where** to draw the line in regard to the populations eligible to receive protection?

2. **How high** to permit the payment standard to rise in high cost markets?

In addressing these questions, we must particularly address the question of how much of our scarce resources we are willing to pay to achieve increasingly higher levels of resident protection.

Prepayment

Mr. Chairman, let me now turn to the issue of prepayment as it relates to the owners. Given that the current approach to preservation cannot be sustained in today's budget environment, I propose that owners of HUD-insured Section 236 and Section 221(d)(3) BMIR low income multifamily rental housing be permitted to prepay their HUD-insured mortgages. Furthermore, I propose that they be permitted to prepay without observing the waiting period prescribed in current law.

With their right to prepay restored, any owner who chooses not to participate or is ineligible to participate can convert their property to market use or continue in their current mode.

TARGETING OF PRESERVATION RESOURCES

As you know, Mr. Chairman, $624 million dollars have been proposed for appropriation for the current program -- but only for the current program. We cannot spend this amount on the new program or an alternative, more efficient approach, such as one we will describe today. This has put us in the curious, if not tragic, position of having to spend a large amount of limited resources on a discredited program, while we must postpone reforms until next year. This unintended result will be pressure to spend scarce resources on a program that doesn't work, leaving no resources for doing the right thing.

I would like to point out, Mr. Chairman, that about 60 percent of the total increase in FY 1997 appropriations over the House level proposed in the Senate bill is targeted to go to the current preservation program. We must thus ask ourselves whether we should allocate that much of our scarce resources to this program.

Mr. Chairman, to state the problem differently, we simply do not have enough money to serve all eligible units under the current preservation law. We are faced with the dilemma of whether it is better to help a very few units at very high costs, or whether it is better to protect residents in all preservation properties. There is simply not enough money to preserve all units. Given this reality, I believe there is no choice but to allow owners to prepay and to protect the low income tenants.

There are those who will point to the 80-year-old widow who may be displaced from her apartment with no apparent place to go and pose the question: Should we allow this person to be displaced? Others will point to a person whose rent is increased substantially, but who remains in place at taxpayers' expense. What I would like to suggest, Mr. Chairman, to underscore the difficulty of sorting this issue out, is that these two descriptions could, in fact, be about the **same** person.

Let me therefore suggest, Mr. Chairman, that we work together to craft an approach that does not defer reforms and that permits us to achieve the basic objectives and principles I stated earlier within the budget resources available to us. That means developing an approach founded on first protecting residents, then permitting prepayments, and finally -- as resources permit -- creating a highly targeted preservation program that uses capital grants and emphasizes sales to resident-controlled entities and public agencies, and requires any other preservation proposals to conform to very narrow criteria, high participation thresholds, real prepayment threat, and solid evidence of local involvement and support.

Mr. Chairman, to the extent that resources are available under the Senate proposal, using Capital Grants and Loans, we estimate that 5,000 units could be preserved for each increment of $100 million in funding:

$100 million -- Would preserve 5,000 Units

$200 million -- Would preserve 10,000 Units

$300 million -- Would preserve 15,000 Units, etc.

We believe this is a fair representation of what your dollars would buy in terms of preservation if applied to a Capital Grant/Loan program, but with no additional resident benefits.

CONCLUSION

Mr. Chairman, the Report of this Committee regarding the Affordable Housing Act of 1990 states that "preservation of the existing inventory for low-income and moderate-income use is a valid and significant component of national housing policy." The Report goes on to state that a Federal preservation strategy, "if structured correctly, can be accomplished in a way that protects the interests of the owners, the tenants and the communities in which the housing is located."

Mr. Chairman, the goals articulated in the original preservation program are still quite valid -- our goals remain the same. What has changed are the fiscal constraints and economic realities of 1995. The challenge for all of us is to continue to strive to achieve these goals within those constraints.

Let me conclude my remarks by restating what I believe to be the three paramount principles that should guide us in our deliberations:

1. We should protect residents currently residing in affordable housing.

2. We should restore the right to prepay.

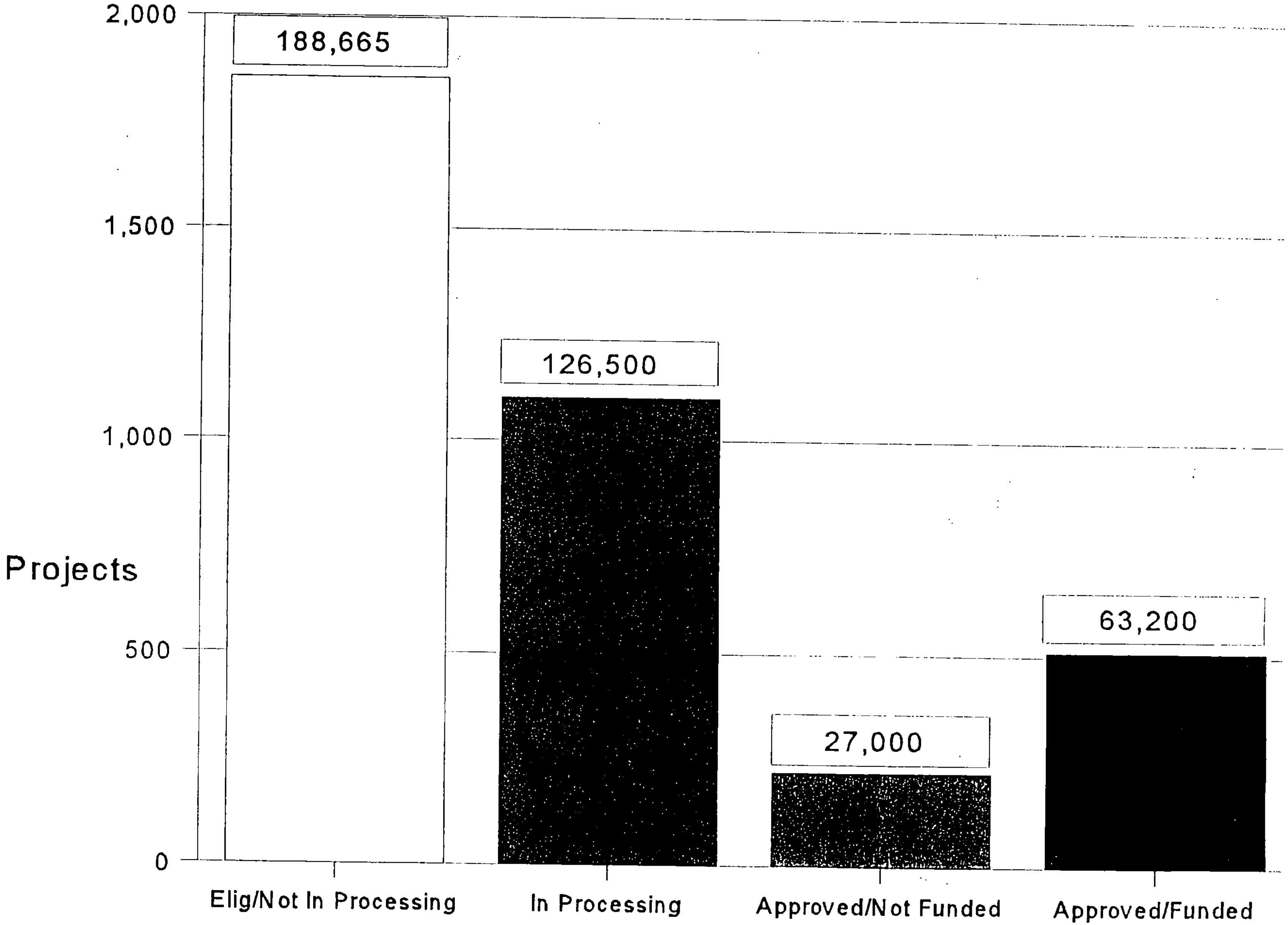
3. We should tightly target any preservation resources that may be available.

As you are aware, Mr. Chairman, funds available for FY 1996 are severely constrained and we must assure that monies available are well-spent. Any monies not well-spent represent dollars that are taken away from somewhere else -- for example, from FHA insurance authority, asset disposition, and public housing.

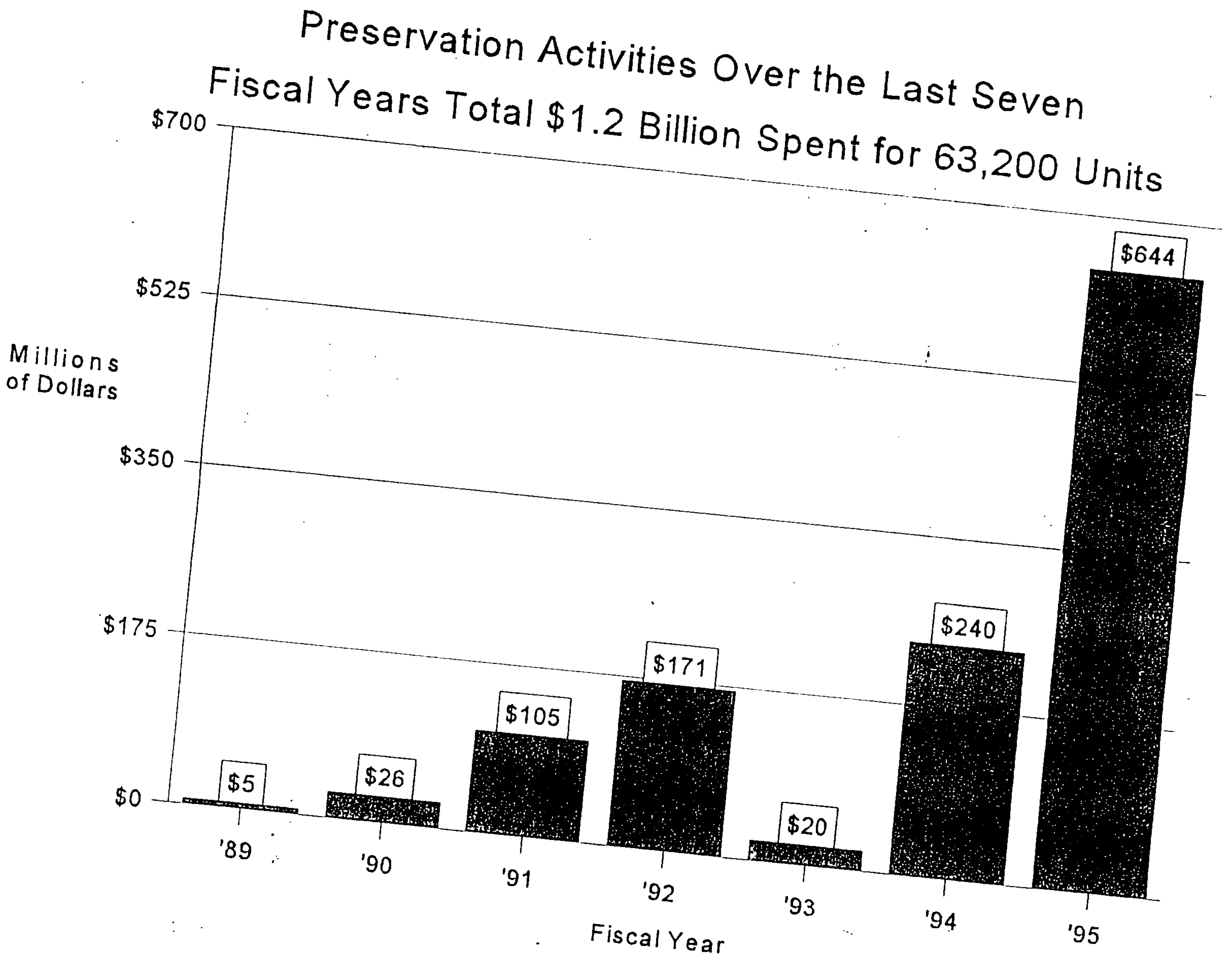
I therefore urge this Committee to adopt an approach such as I have described today.

This concludes my opening statement, Mr. Chairman. I welcome your questions.

Universe of Preservation Projects/Units



NOTE: There are approximately 70,000 non-insured State Agency units that are eligible but have not applied and are not included above.


Preservation Activities Over the Last Seven
Fiscal Years Total $1.2 Billion Spent for 63,200 Units
Millions of Dollars
$700
$525
$350
$175
$0
$5
$26
$105
$171
$20
$240
$644
'89
'90
'91
'92
'93
'94
'95
Fiscal Year

DONALD M. PAYNE
10TH DISTRICT, NEW JERSEY

COMMITTEE ON ECONOMIC AND EDUCATIONAL OPPORTUNITIES

SUBCOMMITTEE ON EARLY CHILDHOOD, YOUTH AND FAMILIES

SUBCOMMITTEE ON EMPLOYER-EMPLOYEE RELATIONS

COMMITTEE ON INTERNATIONAL RELATIONS

SUBCOMMITTEE ON AFRICA

SUBCOMMITTEE ON INTERNATIONAL OPERATIONS AND HUMAN RIGHTS

CONGRESSIONAL BLACK CAUCUS
CHAIRMAN

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October 30, 1995

The Honorable Louis Stokes
United States House of Representatives
2265 Rayburn House Office Building
Washington, DC 20515

Dear Congressman Stokes:

As Chairman of the Congressional Black Caucus, I am writing to express my strong support for the Low Income Housing Preservation and Resident Homeownership Act (LIHPRHA) adopted by the Senate in 1990, and to urge you to place priority on assuring that the preservation program receives sufficient funding when the Conference Committee meets to reconcile the House and Senate HUD/VA/Independent Agencies bills.

I urge the Conferees to appropriate $624 million in Budget Authority for preservation and identify the $440 million in outlays for FY '96 that the Congressional Budget Office has determined are necessary to carry out the reformed program OR support adequate continued funding of the present LIHPRHA program until the authorizing committee can re-design the program. Failure to adequately fund either a redesigned program or the current program will result in prepayments, tenant displacement and the loss of a stock of housing that is considered the best in HUD's portfolio. This policy will devastate many of those who are represented by the Congressional Black Caucus who are pursuing the American dream through homeownership.

Thank you in advance for your consideration of this very important issue and for conveying this message to the Conferees and to the White House.

Sincerely,

Donald

Donald M. Payne, Chairman
Congressional Black Caucus

DMP:pc

Congress of the United States
House of Representatives
Washington, DC 20515

October 23, 1995

The Honorable Jerry Lewis
2112 Rayburn Building
Washington, D.C. 20515

Dear Congressman Lewis:

We are writing to urge your support for adequate funding to maintain the low income housing preservation program when the Conference Committee meets to reconcile the House and Senate VA/HUD/Independent Agencies appropriations bills.

In Massachusetts more than 60 properties containing 12,500 units are being actively processed by HUD for preservation incentives. These include 10 projects that are being sold to resident- and community-based non-profit organizations. In two cases the sales are fully approved, but cannot be consummated due to the lapse in federal funding. If the preservation program is not promptly and adequately funded, this unique opportunity for resident ownership will be lost and the investment of these purchasers and the state and local agencies that have supported them will be totally squandered.

Moreover, because most preservation projects in Massachusetts are viable, well-maintained properties in good locations, many owners are expected to prepay their subsidized mortgages if preservation funds are not made available in a timely manner. Thousands of low and moderate income, predominantly elderly, residents could be displaced at a time when affordable housing options in cities and towns throughout the Commonwealth are dwindling.

Accordingly, we urge you to accept the Senate's decision to appropriate adequate funds to maintain the preservation program, either in its present form, or as a capital grant program (consistent with the House Bill's recommendations). In addition, we also ask that you oppose the Senate provision giving HUD the discretion to stop processing preservation plans and divert all available preservation funding to prepayment vouchers. In Massachusetts' tight housing market, maintaining the existing affordable housing stock at regulated rents is generally more cost-effective than providing tenants with vouchers.

The Honorable Jerry Lewis
Page Two

October 20, 1995

We appreciate your attention to this critical issue affecting the lives of tens of thousands of Massachusetts residents.

Sincerely,

Joe Kennedy
Joseph P. Kennedy II

Peter G. Torkildsen
Peter Torkildsen

Joe Moakley
John Joseph Moakley

Barney Frank
Barney Frank

Richard E. Neal
Richard Neal

Edward J. Markey
Edward Markey

Peter Blute
Peter Blute

Marty Meehan
Marty Meehan

John Olver
John Olver

Gerry Studds

Congress of the United States
House of Representatives
Washington, DC 20515

October 6, 1995

The Honorable Louis Stokes
2265 Rayburn HOB
Washington, D.C. 20515

Dear Congressman Stokes:

We are writing to express our strong support for the reformed Low Income Housing Preservation and Resident Homeownership Act ("LIHPRHA") adopted by the Senate and to urge you to place a priority on assuring that the preservation program receives sufficient funding when the Conference Committee meets to reconcile the House and Senate VA/HUD/Independent Agencies bills. Nearly 500,000 residents in over 150,000 low cost apartments in all 50 states, the District of Columbia, and Puerto Rico are at risk of displacement if the Congress does not appropriate sufficient funding for this program.

More specifically, we are asking that the House recede to the Senate's decision to appropriate adequate funds to maintain the preservation program, either in its present form, or as a capital grant program (consistent with the House Bill's recommendation), which would make it more cost effective. The Senate Bill, if modified to allow for implementation in FY '96, will preserve up to 40,000 units of housing presently occupied by seniors and families that are otherwise at immediate risk of loss, including thousands of units that are being purchased by resident councils and community-based non-profit organizations.

We also wish to note our disagreement with any provisions of the Bill that would result in the conversion of project-based subsidies to tenant-based subsidies. Of particular concern is the provision which grants HUD the discretion to stop processing preservation cases and to allocate all the appropriated funds for housing vouchers upon prepayment rather than for preservation of at-risk housing. While displaced tenants certainly must receive vouchers, it is also critical that the reformed preservation program be fully launched and available to owners and purchasers as a viable alternative to prepayment. In our view, it is more desirable and <u>cost effective</u> to maintain the affordable housing stock that we have developed under these programs at below market rents than it is to provide tenants with a voucher that will be difficult for residents in tight or specialized markets to utilize and are expensive to maintain over time.

The Honorable Louis Stokes
Page Two

We appreciate your vigilance in working to provide funding for housing programs in this difficult climate and we look forward to your efforts in the Conference Committee on behalf of the reformed preservation program.

Sincerely,

JOSEPH P. KENNEDY II

NANCY PELOSI

JOHN BRYANT

JIM MCDERMOTT

RICHARD NEAL

CHARLES SCHUMER

LUIS V. GUTIERREZ

HENRY B. GONZALEZ

THOMAS MANTON

PATSY MINK

MAJOR OWENS

JOSE SERRANO

SIDNEY YATES

LANE EVANS

EDDIE BERNICE JOHNSON

MARTIN FROST

MAURICE HINCHEY

JOHN OLVER

FLOYD H. FLAKE

BOBBY RUSH

LUCIILLE ROYBAL-ALLARD

MAXINE WATERS

WILLIAM H. ORTON

ELIZABETH FURSE

NYDIA VELAZQUEZ

ROBERT MATSUI

LYNN C. WOOLSEY

JERROLD NADLER

THOMAS BARRETT

PETER DeFAZIO

MELVIN L. WATT

JOSEPH P. KENNEDY II
8TH DISTRICT, MASSACHUSETTS

COMMITTEE ON BANKING AND FINANCIAL SERVICES
SUBCOMMITTEES:
HOUSING AND COMMUNITY OPPORTUNITY, RANKING MINORITY MEMBER
DOMESTIC AND INTERNATIONAL MONETARY POLICY

COMMITTEE ON VETERANS' AFFAIRS
SUBCOMMITTEES:
HOSPITALS AND HEALTH CARE
COMPENSATION, PENSION, INSURANCE AND MEMORIAL AFFAIRS

Congress of the United States
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Washington, DC 20515–2108

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(617) 445–1281

October 19, 1995

The Honorable Louis Stokes
2365 Rayburn House Office Building
Washington, D.C. 20515

Dear Mr. Stokes,

Last week, a number of our colleagues sent you a letter expressing their support for continued funding for the Low Income Housing Preservation and Resident Homeownership Act (LIHPRHA). A number of additional colleagues have contacted me to express their interest in supporting this effort. Their names appear below.

Thank you for all your work and leadership on housing issues, and for your efforts on this important program.

Sincerely,

Joe Kennedy

Joseph P. Kennedy II

Kweisi Mfume

Rosa DeLauro

Howard Berman

Henry Waxman

Julian C Dixon

Julian Dixon

George E. Brown, Jr.

George Brown

Vic Fazio

Vic Fazio

Bob Filner

Bob Filner

Sam Farr

Sam Farr

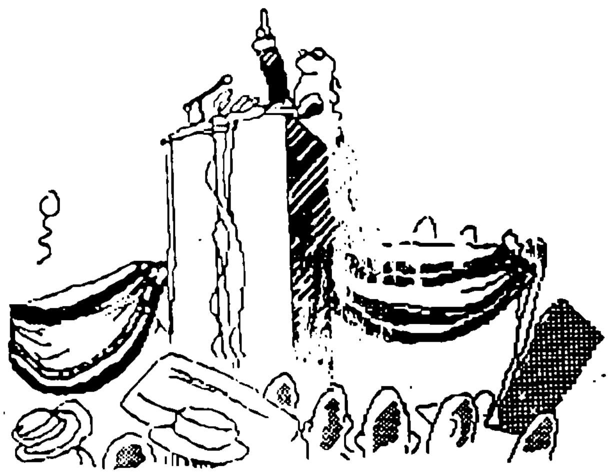
Jane Harman

Jane Harman

Esteban E. Torres

Esteban Torres

EXECUTIVE OFFICE OF THE PRESIDENT
Office of Management and Budget



FACSIMILE TRANSMITTAL SHEET

Number of pages including cover 14

Date: 10/30/95

To: Molly Brostrom

Fax Number:

Office Number:

Comments: Background on HUD Preservation

HOUSING BRANCH

From: **ADAM HOFFBERG**

Fax Number: **(202) 395-1307**

Office Number: **(202) 395-1094**

10-13-95
4:00 PM

STATEMENT OF

NICOLAS P. RETSINAS
ASSISTANT SECRETARY FOR HOUSING - FEDERAL HOUSING COMMISSIONER

Before the

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
SUBCOMMITTEE ON HOUSING OPPORTUNITY & COMMUNITY DEVELOPMENT
UNITED STATES SENATE

October 17, 1995

Mr. Chairman and Members of the Committee:

Thank you for inviting me here today to participate as a partner with you in our mutual efforts to improve the way we preserve affordable housing opportunities. In my brief remarks, I would like to share with you some facts and numbers which tell where we are today and what is at stake regarding the issue of preservation. Finally, I would like to suggest for your consideration some core principles to guide us in our deliberations.

Prior to assuming my position with HUD as Assistant Secretary for Housing, I co-authored an article about preservation, especially as it relates to Elderly housing. At that time, I predicted that the current legislation might not work easily or efficiently. I now know first-hand the wisdom of that earlier prophecy.

When we crafted the current preservation language -- and I say "we" because many of us in this room were involved -- we envisioned a crisis which would result in the loss of hundreds of thousands of units of affordable housing and the diplacement of thousands of residents. The existing preservation program was a noble effort to forestall that problem. Now, however, with the benefit of hindsight, we are able to see the problem more clearly and also to see the strengths and weaknesses of the program we crafted.

Thus, my comments are not meant to criticize or denigrate the important efforts of all who participated in developing the program. Rather, we can use our experience to strengthen what we do in the future in this environment of constrained resources.

BACKGROUND ON CURRENT PROGRAMS

Building on interim legislation enacted in 1987, the Congress developed an approach that practically precluded any prepayments and promised to pay virtually any price to achieve that objective. That strategy set up a procedure that restricts owners' prepayment rights or, as some have argued, closely resembled an eminent domain taking process. In any event, the procedure was complex and detailed, including multiple appraisals, with no practical limits on costs.

The existing program relies on two fundamental subsidies: increased debt, insured by the FHA fund and increased Section 8 subsidies, to support this debt. By doing this, we increased the long term liabilities of the federal government, through the FHA insurance fund, sometimes extending far beyond the Section 8 subsidy commitment. To put numbers on this, we have created 35,000 new units of Section 8 subsidy, costing approximately $230 million a year, in addition to Section 8 subsidy supplements to units already in place.

27,000 units

Today, 227 approved preservation Plans of Action are waiting to be funded at over $700 million in new budget authority. One could argue, Mr. Chairman, that preservation has achieved its objectives -- but at a current and future cost that we can no longer afford if indeed we ever could.

STATUS OF PRESERVATION PIPELINE

There is a certain irony in the fact that we have increased by tenfold the number of projects processed in any given year during our administration. In the four years from 1989 to 1993, we processed only 120 projects. In 1994 alone, we processed an additional 120 projects. And in 1995, we processed 268 projects, or double the 1994 level.

Approved Projects

Since the beginning of the current laws on preservation, we have approved Plans of Action for 738 projects through September 30th of this year. These projects represent just under 90,000 units, broken down as follows:

- 511 projects, with approximately 63,000 units, were approved and funded at a cost of $1.2 billion -- but only for the first five years of preservation. This cost has to be continued for at least the full remaining term of the mortgage.

- Another 227 projects, with 27,000 units, are in the unfunded pipeline queue. The total cost of funding these projects would be over $700 million.

Projects In Processing

There are an additional 1,100 projects with 126,500 units that are in processing. Slightly more than 800 of thesed projects have not reached the completion of their appraisal process, with the remainder awaiting plan of action approvals. If all of these projects were to be approved -- clearly, not all of them would -- the total cost to the taxpayers, based on current cost experience, would be almost $2.5 billion.

Eligible Projects Not In Processing

As for eligible projects not in processing, there are 1,855 insured projects with 188,665 units that have not initiated any filing under the preservation program. Additionally, it is believed that there are approximately 70,000 units of State Agency non-insured projects that have not filed.

BASIC PRINCIPLES OF REFORM

Mr. Chairman, notwithstanding this status report, numbers alone do not fully capture the overriding budget issue that is driving the preservation policy debate. We believe that our current efforts at preservation are too costly and cannot be sustained given today's budgetary realities. Therefore, Mr. Chairman, if the current approach is simply too costly, how do we proceed from here?

We have learned a number of lessons from our experience in administering Titles II and VI. We wish to apply the lessons gained from our experience in such a way as to protect residents from adverse consequences of our actions in this area. My principal concern as Assistant Secretary for Housing and Federal Housing Commissioner is to assure that existing residents continue to reside in affordable rental housing.

Fundamental to reforming Preservation is changing the priorities from owner compensation to resident protection. This means that, as the owners' right to prepay is restored, the residents must be protected from any threats that may arise to their continued residency.

<u>Quotes from Inspector General</u>

Mr. Chairman, let me quote from a recent report of our Inspector General's office regarding the Multifamily Preservation Program:

"We believe that the Preservation Program should be repealed, thereby eliminating the project owner's ability to obtain equity from the project without taking any risk. Repeal would also eliminate the need for additional project-based subsidies. Project owners would be allowed the uncontested option

of prepayment and tenants would be provided tenant-based subsidies, giving them the freedom to choose where to live."

Quoting from the same report dated July 14, 1995, the IG's office states:

"HUD has an opportunity to make a clean break from policies and programs that failed in the past and to pursue new approaches to old problems that hav long beset HUD's Multifamily Programs. As this study points out, there is no easy solution to the preservation problem. However, **the cornerstone for correcting the problem, both from the cost and legal aspects, must include the uncontested option for the project owner to prepay as HUD's proposed "New Preservation" program does. Prepayment allows the greatest flexibility for the market to establish both the rents for tenants and the value of the project for the owners.**"

Mr. Chairman, cognizant of these findings by HUD's Inspector General, I believe there are certain actions we can and should take to reform and improve the Preservation Program, and I would like to review with you those actions or guiding principles.

1. **Protect residents.** The first action relates to my foremost concern, Mr. Chairman, and that is resident protection. I know that you share this concern. Whatever course of action is taken, residents must come first. The protection of residents can be achieved in part by the provision of vouchers. I will elaborate on that in a few moments.

2. **Restore the right to prepay.** Secondly, if we agree that, under the current budget realities, the current approach to preservation is too costly, we must restore the right of owners to prepay their mortgages. As stated before, to do otherwise leads to an expensive and convoluted process.

AN APPROACH

With these principles in mind, let me suggest a possible approach for your consideration, Mr. Chairman, that would encompass all of these principles.

Protection of Residents

In the case of prepayments, current contracts would continue as project-based until they expire and, when they do expire, the same policies as for other contract expirations would apply.

Additional eligible residents would be provided with tenant-based Section 8 rental assistance in the form of vouchers. Income eligibility of residents receiving these vouchers would continue to be up to 80 percent of area median income, the same as current law for these projects.

Actual 450
425
FMR 400

Normal Section 8 Voucher Payment Standards would prevail for residents currently in place at the time of prepayment, except that, if actual rent levels were higher than the ~~Payment Standard~~, the payment would be increased up to the actual rent level, but not ~~exceeding comparable market rents~~ in that area.
Fair Market Rent

All eligible residents would qualify for this benefit as long as they remain in residency, provided appropriations continue. Owners would be barred from evicting these residents as long as they are lease compliant. If the resident moves, the voucher goes with them, but at a reduced level of subsidy.

FMR 400
Project 300
200

Prepayment

Mr. Chairman, let me now turn to the issue of prepayment as it relates to the owners. Given that the current approach to preservation cannot be sustained in today's budget environment, I propose that owners of HUD-insured Section 236 and Section 221(d)(3) BMIR low income multifamily rental housing be permitted to prepay their HUD-insured mortgages. Furthermore, I propose that they be permitted to prepay without observing the waiting period prescribed in current law.

With their right to prepay restored, any owner who chooses not to participate or is ineligible to participate can convert their property to market use or continue in their current mode.

COST COMPARISON

Mr. Chairman, I would now like to compare the costs of the Senate's proposal with the costs associated with the approach I have just outlined.

Outlays under the Senate proposal are quite high initially -- $1.9 billion over the next five years, based on our estimates -- because owners receive Capital Grants/Loans as soon as Plans of Action are approved. By comparison, our proposal extends long-term protection directly to eligible tenants and costs much less -- $800 million.

The situation changes over time, however. Unlike current legislation which provides assistance to all eligible low-income and very low-income tenants, the Senate bill limits assistance to only families now receiving Section 8. We propose to continue assistance to all eligible families after prepayment, and because we help more families, the costs of our proposal rises over time relative to the Senate approach. In nominal dollars, by the year 2009, the cumulative costs of the Senate and Administration proposals are approximately equal and, after that date, the Senate approach -- which would still assist fewer households -- costs less. On a present value basis, our proposal would actually cost less through the year 2015.

To summarize, what the Senate proposal buys at a higher initial cost, is project or unit based preservation. Whereas, the Administration's proposal, with its lower initial but gradually rising cost, provides protection and choice to a greater number of residents at a lesser net present value cost over the next 20 years. The cost of our approach over the longer term -- i.e., beyond 20 years -- can be expected to continue to rise relative to the approach proposed by the Senate.

TARGETING OF PRESERVATION RESOURCES

As you know, Mr. Chairman, $624 million dollars have been proposed for appropriation for the current program -- but only for the current program. We cannot spend this amount on the new program or an alternative, more efficient approach, such as one we will describe today. This has put us in the curious, if not tragic, position of having to spend a large amount of limited resources on a discredited program, while we must postpone reforms until next year. This unintended result will be pressure to spend scarce resources on a program that doesn't work, leaving no resources for doing the right thing.

Mr. Chairman, to state the problem differently, we simply do not have enough money to serve all eligible units under the current preservation law. We are faced with the dilemma of whether it is better to help a very few units at very high costs, or whether it is better to protect residents in all preservation properties. There is simply not enough money to preserve all units. Given this reality, I believe there is no choice but to allow owners to prepay and to protect the low income tenants.

There are those who will point to the 80-year-old widow who may be displaced from her apartment with no apparent place to go and pose the question: Should we allow this person to be displaced? Others will point to a person who is paying three times as much as they should be -- and at taxpayers' expense -- by staying in the same place. What I would like to suggest, Mr. Chairman, to underscore the difficulty of sorting this issue out, is that these two descriptions could, in fact, be about the same person.

Let me therefore suggest, Mr. Chairman, that we work together to craft an approach that does not defer reforms and that permits us to achieve the basic objectives and principles I stated earlier within the budget resources available to us. That means developing an approach founded on first protecting residents, then permitting prepayments, and finally -- as resources permit -- creating a highly targeted preservation program that uses capital grants and emphasizes sales to resident-controlled entities and public agencies, and requires any other preservation proposals to conform to very narrow criteria, high participation thresholds, real prepayment threat, and solid evidence of local involvement and support.

Mr. Chairman, to the extent that resources are available under the Senate proposal, using Capital Grants and Loans, we estimate that 5,000 units could be preserved for each increment of $100 million in funding:

$100 million -- Would preserve 5,000 Units

$200 million -- Would preserve 10,000 Units

$300 million -- Would preserve 15,000 Units, etc.

We believe this is a fair representation of what your dollars would buy in terms of preservation if applied to a Capital Grant/Loan program, but with no additional resident benefits.

CONCLUSION

Mr. Chairman, the Report of this Committee regarding the Affordable Housing Act of 1990 states that "preservation of the existing inventory for low-income and moderate-income use is a valid and significant component of national housing policy." The Report goes on to state that a Federal preservation strategy, "if structured correctly, can be accomplished in a way that protects the interests of the owners, the tenants and the communities in which the housing is located."

Mr. Chairman, the goals articulated in the original preservation program are still quite valid -- our goals remain the same. What has changed are the fiscal constraints and economic realities of 1995. The challenge for all of us is to continue to strive to achieve these goals within those constraints.

Let me conclude my remarks by restating what I believe to be the three paramount principles that should guide us in our deliberations:

1. We should protect residents currently residing in affordable housing.

2. We should restore the right to prepay.

3. We should tightly target any preservation resources that may be available.

As you are aware, Mr. Chairman, funds available for FY 1996 are severely constrained and we must assure that monies available are well-spent. Any monies not well-spent represent dollars that are taken away from somewhere else – for example, from FHA insurance authority, asset disposition, and public housing.

I therefore urge this Committee to adopt an approach such as I have described today.

This concludes my opening statement, Mr. Chairman. I welcome your questions.

[276] From: Stephen A. Martin at FHCPOST3 9/12/95 9:49AM (4838 bytes: 86 ln)
To: Chris Greer at OIGPOST2, Steve Redburn at BIGPOST
cc: Alan Schwartz at THG-POBOX, Nancy O. Andrews, Helen M. Dunlap,
carlap.hrcd@cbo.gov at Internet
Subject: Thoughts on David's Pres Model
------------------------------ Message Contents ------------------------------
Attached is the analysis of Cap Grants/Loans to which Helen referred.

Helen:

I've done some thinking about David's arguments on Pres. I believe that his position is logically flawed: at one point, he argues that the ownership issue (Pres) and the fate of tenants after expiration of LMSA (MtM) should be kept separate. For Pres, therefore, he counts only the cost of the grant/loan. But in comparing Pres to non-Pres, he wants to count the cost of assisting the tenants--but he can't have it both ways: to be fair, the comparison should either be (a) ownership cost/benefits only, or (b) ownership and tenant cost/benefits combined for both options. Comparing the cost of Pres with the cost of Vouchers is mixing apples and oranges.

1. The Senate version of Pres will provide a windfall benefit to a large number of owners for little benefit to tenants.

The starting point is "What is this project's highest and best use?" Projects that are more valuable as condos are history. For those that are best suited for rentals, there are now some number of potential bidders. What Cap Grants does is expand the number of potential bidders by providing funding to nonprofits. Increasing the demand while the supply stays constant will inevitably lead to higher sales prices--thus, sellers benefit from the availability of grants, but at a cost to the taxpayer. Similarly, Cap Loans provide low cost financing for stayers, a benefit to owners who agree to maintain the Section 236 or BMIR income limits--but again, this benefit goes to all owners, even those who would have rented to these families anyway! If the market of my project is for low income renters at, say 60-80% of income, the grant/loan is a pure windfall: I get a higher price at sale or a cheaper loan merely for doing what I would have done anyway--serve my market.

The benefits of Pres are: (1) some number of projects that would have been sold to profit motivated owners are now owned by nonprofits, and (2) in some instances, units that would have been occupied by families earning, say, 92% of median income will instead be occupied by families earning only 78% of median. At the margin, there will be a small expansion of the supply of rental units for the higher end of the low income scale.

The problem is that these benefits are not particularly dramatic and probably not worth the cost to the taxpayer. So instead, David says "Look how much more expensive it will be to make these units affordable to the very poor." It's probably unfair to say that the Administration proposal (MtM) seeks to protect the tenants and says to hell with the owner, while the industry proposal (Pres) seeks to protect the owner and says to hell with the tenant--but Pres alone does nothing for the needy poor. Comparing the cost of inducing owners to rent to families earning 80-90% of median (Pres) with the cost of assisting families earning 20-30% of median (Vouchers) is meaningless.

2. The real alternative cost to Pres is zero.

If one truly treats the fate of current LMSA tenants as a separate issue for purposes of analysis, the alternative to Pres is to do nothing. Owners who want to sell will still sell--but fewer nonprofits will be able to buy. Owners who want to stay but need cash will still be able to borrow--but will have to do so at market rates.

If the industry intends to protect very low income tenants after the expiration of LMSA, the comparison would then be grants plus tenant protections vs. no grants & tenant protections. In the HUD model, I've given the industry the benefit of doubt and price Pres on the assumption that LMSA continues. An equally likely possibility is:

** The owner receives a Cap Grant/Loan,
** The owner continues to receive Sec. 236 (stayers), and
** Tenants receive Vouchers after the current LMSA

contract expires.

In the event, the cost would be Grant + Voucher or Loan + Section 236 + Voucher versus the Administration's proposal of Voucher only. Which do you think is more expensive?

Steve M.

[277] From: Chris Greer at OIGPOST2 9/12/95 9:47AM (2074 bytes: 35 ln)
To: Stephen A. Martin at FHCPOST3, Helen M. Dunlap at FHCPOST3,
CARLA PEDONE <carlap.hrcd@cbo.gov> at Internet
cc: CONRAD EGAN at FHCPOST3, Paul A. Leonard at PDRPOST, Steve Redburn at BIGPOST, Richard A Hale at GAO, Chris Greer, David J. Derecola, Stanley J. McLeod
Subject: Re[3]: Impact of Capital Grants/Loans on Tenants

---------------------------- Message Contents ----------------------------

Steve-- I just reviewed your document. It is marvelous and a compelling argument against the industry proposal from any reasonable standpoint. Thanks.

A short summary of the worksheet and my earlier analysis:

** Capital Grants/Loans and Vouchers are NOT interchangeable. A simple comparison of the cost of one versus the other ignores the fact that they do different things.

** Capital Grants increase the number of potential buyers for preservation properties by enabling nonprofits to bid on eligible properties--but DO NOTHING to alleviate tenant rent burden.

** Capital Loans provide interest free loans to current owners--and in the absence of tenant subsidies actually CAUSE RENT BURDEN TO RISE!

** Vouchers benefit very low income tenants directly: they enhance their buying power and give them the freedom to choose where to live.

** A choice of Capital Grants/Loans ONLY will benefit current owners and nonprofit purchasers AT THE EXPENSE OF THE TENANTS.

** A choice of Capital Grants/Loans PLUS Vouchers will make everyone happy--but at a cost we can't afford.

** A choice of Vouchers only will protect the tenants by expanding their buying power, and subject the owners to market discipline.