The original documents are located in Box 1, folder "Budget (FY1977) - HUD" of the Richard B. Cheney Files at the Gerald R. Ford Presidential Library.

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

MEETING ON FY-1977 BUDGET
Thursday, November 13, 1975
3:00 p.m. (60 minutes)
Oval Office

From: James T. Lynn

I. PURPOSE

To make decisions on issues raised by the FY-77 budget for the Department of Housing and Urban Development.

II. BACKGROUND, PARTICIPANTS AND PRESS PLAN

A. Background: The FY-77 budget submission of the Department of Housing and Urban Development has been reviewed by the Office of Management and Budget and members of the White House staff. This meeting will focus on an issue raised in the budget submission that requires Presidential consideration and determination.

B. Participants: James T. Lynn, James Cannon, Paul O'Neill, and Dale McOmber.

C. Press Plan: David Kennerly photo

III. TALKING POINTS

A. Paul, what is the first issue we should discuss today?

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

NOV 12 1975

ACTION

MEMORANDUM FOR: THE PRESIDENT

FROM: James T. Lynn

SUBJECT: 1977 Budget Decisions: Department of Housing and Urban Development

The agency requests and my recommendations with respect to 1977 budget amounts for the Department of Housing and Urban Development are presented in the tabulation attached (Tab A). A summary of the principal budget decisions reflected in my recommendation is provided as background information (Tab B).

Four key issues have been identified for your consideration (additional detail at Tab C).

I. SUBSIDIZED HOUSING

Secretary Hills recommends that the budget provide for 400,000 units under the Section 8 rental housing program. She acknowledges, however, that additional sweeteners (e.g., subsidies under the Tandem Plan, longer subsidy terms, aid to State housing agencies) are needed if the 240,000-unit target for new construction is to be achieved.

OMB recommends approval for 245,000 units under Section 8, of which only one-third would involve new construction. When added to the 130,000 units under the reactivated Section 235 program, subsidized housing activity would be only slightly below the 400,000 level contained in the 1976 Budget. We believe Section 8 support for new construction should be kept as close to zero as politically feasible, given the staggering costs anticipated under this program. (In our view, this issue is closely linked to the Tandem Plan issue which has been put before you in a separate memorandum.)

II. MORTGAGE MODIFICATION

HUD has proposed a new policy toward subsidized housing projects with nonprofit sponsors that, in effect, would forgive 75 percent of the required mortgage payments. The Secretary believes such relief is necessary to maintain the stock of subsidized housing and avoid a congressionally mandated program of operating subsidies.

OMB recommends against the proposed policy on the grounds that it would increase outlays sharply without removing the threat of operating subsidies. Furthermore, we recommend that HUD take a hard line toward projects in default, foreclosing where they cannot be made current and reselling (with Section 8 assistance for present tenants) to the highest bidder.

We are still discussing this issue with HUD, and our recommendation could change if convincing evidence to support the Department's position is developed.

III. PUBLIC HOUSING OPERATING SUBSIDIES

HUD recommends continuing the present system of funding public housing operating deficits, without change.

OMB recommends revising the present system to provide for greater tenant contributions to cover operating costs. Although these changes would increase median rents by 28 percent, no family would be expected to pay more than 25 percent of its gross income.

IV. COMPREHENSIVE PLANNING GRANTS ("701")

HUD reduced its original budget request for planning grants from $100 million to $50 million as part of its outlay reduction plan. The funds would be directed towards regional organizations so that required housing and land use plans may be completed, qualifying the organizations for future planning assistance. HUD also sees the program as a receptacle for consolidating several Federal planning programs under central management of the 701 organization to increase efficiency and coordination and decrease Government overhead costs.

OMB recommends folding the 701 program into the Community Development Block Grant Program in 1977. There are adequate funds available under the block grant program to support 701 activities, and these funds go to chief executives rather than regional organizations lacking governmental authorities. Numerous attempts to devise a strategy to consolidate Federal planning programs have been unsuccessful.

Attachments

Recommendations
and Reductions

TAB A

1977 Budget

Department of Housing and Urban Development

Summary Data

	(In Millions) Budget Authority*	Outlays	Employment, end-of-year Full-time Permanent	Total
1975 actual	15,550	7,488	15,142	16,881
1976 February budget	21,239	7,055	15,200	17,174
enacted	25,879	7,810	xxx	xxx
HUD request	25,881	7,812	15,060	16,985
OMB recommendation	24,862	7,383	14,960	16,885
TQ February budget	341	1,905	xxx	xxx
enacted	626	2,140	xxx	xxx
OMB recommendation	347	1,947	xxx	xxx
1977 planning target	35,799	8,000	xxx	xxx
HUD request	51,773	8,613**	16,222	17,847
OMB recommendation	7,361	7,453	15,414	17,039
1978 OMB estimate	29,198	8,302	15,414	17,039

* Revised to show budget authority for long-term subsidy programs on a consistent basis.
** The Secretary would offset $613 million through the sale of assets ($600 million) and miscellaneous reductions.

1977 Budget
Department of Housing and Urban Development
Summary of Recommended Program Reductions
($ in millions)

	1976		TQ	1977			1978	
	0	FTP Employ.	0	BA	0	FTP Employ.	0	FTP Employ.
Current base	7,604	15,375	2,022	45,023	8,103	16,411	9,978	16,617
Recommended level	7,383	14,960	1,947	7,361	7,453	15,414	8,302	15,414
Reduction	221	415	75	37,662	650	997	1,676	1,203
Program reductions:								
Section 8/subsidized housing - reduce new construction	---	434	---	30,195	---	1,056	544	1,017
Comprehensive Planning - terminate program	---	---	---	75	15	106	68	106
Rehabilitation Loans - terminate program (legislation required)	21	60	32	50	68	60	70	60
Section 802/Grants to State Housing Agencies - rescind 1976 appropriation (legislation required)	---	---	---	600	---	20	15	20
GNMA: Special Assistance Functions - no new tandem purchases	---	---	---	5,000	42	---	595	---
Mortgage insurance programs:								
Accelerate foreclosures	---	---	---	118	118	-104	90	---
Accelerate sale of single-family properties	159	-79	42	261	261	-163	---	---

	1976		TQ	1977			1978	
	0	FTP Employ.	0	BA	0	FTP Employ.	0	FTP Employ.
Raise premiums to actuarially sound levels..................	---	---	---	18	18	---	26	---
Salaries and Expenses - reductions made possible by program cuts..................	1	xxx	1	10	10	xxx	10	xxx
Payments for Operation of Low-Income Housing Projects: Eliminate deductions from gross income (legislation required)....................	---	---	---	87	25	---	79	---
Increase rent base: terminate Target Projects Demonstration Program......................	---	---	---	114	23	22	84	---
Housing for the elderly - reduce loan level (off-budget)........	(---)	(---)	(---)	(160)	(---)	(---)	(24)	(---)
Rent supplements - make no amendments to existing contracts.....................	---	---	---	800	10	---	25	---
College Housing - terminate program (legislation required)....................	40	---	---	334	60	---	70	---
Total reductions.............	221	415	75	37,662	650	997	1,676	1,203

1977 Outlay Reductions
Department of Housing and Urban Development
Rehabilitation Loans
(dollars in millions)

	1976		TQ	1977			1978	
	O	FTP employ.	O	BA	O	FTP employ.	O	FTP employ.
Amount:								
Current base........	76	60	29	50	50	60	50	60
Recommended level...	55	0	-3	0	-18	0	-20	0
Reduction.........	21	60	32	50	68	60	70	60

Action required:

Rescission of all balances available for the Rehabilitation Loan program.

Program impact:

The Rehabilitation Loan program adds no authority to what is already available in the Community Development Grant program. HUD estimates that community development grant funds going to rehabilitation will total about $307 million in 1976 and $350 million in 1977. These amounts are far greater than any one year's funding for the Rehabilitation Loan program during its 10-year existence as a categorical program.

Other considerations:

This action will not be accepted easily by either big city mayors or the Congress.

1977 Outlay Reductions
Department of Housing and Urban Development
Section 802 Assistance to State Housing Agencies
(dollars in millions)

	1976			TQ	1977			1978		
	BA	O	FTP employ.	O	BA	O	FTP employ.	BA	O	FTP employ.
Amount:										
Current base............	600	0	1/	0	600	0	20 2/	600	15	20 2/
Recommended level.......	0	0	1/	0	0	0	0	0	0	0
Reduction.............	600	0		0	600	0	20	600	15	20

1/ HUD proposes to absorb the 1976 operation within current ceilings.
2/ OMB estimate of staffing for ongoing program.

Actions required:

Propose rescission of the $15 million appropriated to liquidate contract authority in 1976 for interest subsidies to State housing and development agencies. Request no appropriations for 1977 and beyond. Do not implement the loan guarantee provision.

Program impact:

Implementing the interest subsidies and loan guarantees would decrease the borrowing costs of State agencies at the margin. These decreased costs would induce State agencies to construct more subsidized housing for low- or moderate-income households. Most immediately, it would increase the new construction component of the Section 8 Lower Income Housing Assistance Program above what it otherwise would be.

States could reduce borrowing costs for their agencies by a greater amount in the aggregate by pledging their "full faith and credit" to the agency borrowing. However, States are unlikely to do this in any great number.

To the extent federally sponsored new construction for low-income households is desired, not implementing Section 802 would shut off a potential resource to assist in the administrative burden of the Section 8 program.

Other considerations:

Rescission would be very difficult to accomplish. Congress appears determined to insure the role of State agencies in constructing subsidized housing and to provide some financing mechanism for new construction under the Section 8 program.

1977 Outlay Reductions
Department of Housing and Urban Development
Mortgage Purchase Assistance (Tandem) Program
(dollars in millions)

	1976		TQ	1977			1978	
	0	FTP employ.	0	BA	0	FTP employ.	0	FTP employ.
Amount:								
Current base............	0	---	0	5,000	42	---	595	---
Recommended level.......	0	---	0	0	0	---	0	---
Reduction.............	0	---	0	5,000	42	---	595	---

Actions required:

Do not release any of the $5 billion in standby mortgage purchase authority currently available, and request no new authority for 1977 or later.

Program impact:

The Tandem program provides an interest subsidy, inducing housing construction at the margin. OMB is pessimistic that the program has any appreciable impact on the volume of housing starts. Most of the subsidized construction starts would occur anyway. Many others would represent starts pushed forward from future time periods.

Other considerations:

The Tandem funds are standby funds, and their release is at the discretion of the Administration. This flexibility provides political advantages in timing and/or targeting Tandem assistance to meet sudden political and/or economic needs.

1977 Outlay Reductions
Department of Housing and Urban Development
Acquired Property Sales
(dollars in millions)

	1976		TQ	1977			1978	
	0	FTP employ.	0	BA	0	FTP employ.	0	FTP employ.
Amount:								
Current base.......	-710	1,038	-177	-706	-706	990	-706	990
Recommended level..	-869	1,117	-219	-967	-967	1,153	-706	990
Reduction........	159	-79	42	261	261	-163	0	0

Actions required:

Increase the sales targets for the disposition of single-family property acquired in FHA's mortgage insurance operations.

Program impact:

Sales targets would be increased to 85,000 (from 73,000) in 1976 and 100,000 in 1977. The acquired property inventory would decline to 60,000 units in 1977 instead of increasing to 110,000 units. The increased sales of acquired single-family homes would require greater emphasis on the "as-is" sales approach relative to the "repair and reinsure" approach. As-is sales result in the highest return to the FHA Fund and a quicker disposition of units from the inventory. However, deemphasizing the repair and insure approach would reduce the use of Federal money for rehabilitation.

Other considerations:

Confrontations with public interest groups and city officials would increase if heavy use of the as-is sales approach occurred in particular neighborhoods. Neighbors and city officials would be pleased to the extent that the units were privately rehabilitated and occupied faster than they would be with the repair and insure approach.

1977 Outlay Reductions
Department of Housing and Urban Development
Federal Housing Administration (FHA) Fund/Mortgage Insurance Premiums
(dollars in millions)

	1976		TQ	1977			1978	
	0	FTP employ.	0	BA	0	FTP employ.	0	FTP employ.
Amount:								
Current base............	-463	---	-125	-466	-466	---	-466	---
Recommended level.......	-463	---	-125	-484	-484	---	-492	---
Reduction.............	0	---	0	18	18	---	26	---

Actions required:

Administratively increase mortgage insurance premiums to actuarially sound levels (up to the legal maximum annual rate of 1 percent) for each FHA mortgage insurance program.

Program impact:

The change in premiums would be small and it is unlikely that the impact on demand would be significant, although the volume of insurance could decrease a small amount. Low-income and minority families are proportionately heavier users of the riskier insurance programs where premiums would be increased the most. HUD believes the increased premiums would "...cause some groups to delay home purchase." The Section 235 program would be reactivated in January with an actuarially sound premium.

Other considerations:

Mortgage bankers, homebuilders, realtors, and others in the real estate industry have become accustomed to the flat premium. The Section 235 premium is under an intensive review by HUD so a January change is possible. HUD could review the other premium levels with interested private parties and the Congress before changing premiums on July 1, 1976.

1977 Outlay Reductions
Department of Housing and Urban Development
Housing for the Elderly
(dollars in millions)

	1976		TQ	1977			1978	
	O	FTP employ.	O	BA	O	FTP employ.	O	FTP employ.
Amount (off budget):								
Current base.......	(-15)	---	(-4)	(375)	(132)	---	(359)	---
Recommended level..	(-15)	---	(-4)	(215)	(132)	---	(335)	---
Reduction.......	(0)	---	(0)	(160)	(0)	---	(24)	---

Actions required:

Reduce the annual loan level for Section 202/Housing for the Elderly from $375 million for permanent financing to $215 million for construction loans.

Program impact:

The $160 million reduction would reduce the number of elderly housing units assisted from 15,000 to 8,600 units. Nonprofit sponsors would have to obtain permanent financing from other sources (e.g., FHA 100-percent insured loans), and pay the market interest rates. However, the interest differential is less than one-half percent, and the impact on rent levels would be minimal. At current rates, the difference in rent required would be $9 per month which would lower tenant income requirements by less than $500 per year. Treasury borrowing needed to finance $375 million in permanent loans would raise interest on the national debt by approximately $20 million. The proposed construction loan approach would avoid the pyramiding of long-term debt and much of the increased borrowing costs since the loans would be repaid in 2 years rather than 40.

Other considerations:

Elderly housing has been one of the most emotional issues in Federal housing policy. Nonprofit sponsor and elderly interest groups have been effective in obtaining legislation that the Administration opposed.

1977 Outlay Reductions
Department of Housing and Urban Development
Rent Supplements
(dollars in millions)

	1976		TQ	1977			1978	
	O	FTP employ.	O	BA	O	FTP employ.	O	FTP employ.
Amount:								
Current base.......	210	---	60	800*	268	---	305	---
Recommended level..	210	---	60	---	258	---	280	---
Reduction........	0	---	0	800*	10	---	25	---

* $20 million in contract authority times the 40 year project life.

Actions required:

Do not request the release of any contract authority for rent supplements after 1976.

Program impact:

If additional rent supplement authority is not provided to underwrite operating costs and rent increases, tenants would either have to pay increased rents or move. If too many tenants moved and the owner could not find replacements, the mortgage might go into default and be assigned to HUD. There is no basis for estimating the volume or cost of these assignments. The assigned mortgage could be foreclosed and sold at a loss.

Adopting a policy of matching operating cost increases with Federal subsidies weakens incentives for good management. It would also increase subsidies going to those relatively few families already being subsidized heavily, while comparable families receive no subsidies.

Other considerations:

Since the rent supplement program serves mainly low income households, the President will be criticized as being unconcerned with the welfare of these tenants. Pressure to provide additional rent supplement authority after 1976 will come from low income and minority groups and some Congressmen.

1977 Outlay Reductions
Department of Housing and Urban Development
College Housing Loans
(dollars in millions)

	1976		TQ	1977			1978	
	0	FTP employ.	0	BA	0	FTP employ.	0	FTP employ.
Amount:								
Current base..................	10	---	-15	---	---	---	---	---
Recommended level.............	-30	---	15	-334	-60	---	-70	---
Reduction..................	40	---	0	334	60	---	70	---

Actions required:

Rescission of all funds available for direct loans.

Program impact:

Recent studies have shown that there is no current need for a national College Housing Program--a point the House Appropriations Committee acknowledges. Moreover, subsidized loans financing dormitory construction represent an inefficient means of carrying out the Administration's higher eduction policy. Such loans favor rich and poor students alike, and discriminate against day students and students who live off campus.

Other considerations:

Individual colleges have lobbied for continuation of the loan program in order to finance additional construction or modernization of existing dormitories. Favorable action by the Congress will be difficult to achieve.

Summary of Budget Decisions

TAB B

1977 Budget
Department of Housing and Urban Development

Summary of Principal Budget Decisions
Reflected in the OMB Recommendations

Fiscal Year 1976

Mortgage Purchase ("Tandem") Program

In a separate memorandum, HUD has proposed release of $3 billion in mortgage purchase authority for multifamily housing.

OMB has recommended against release of this authority, and the budget totals presented under Tab A do not include any outlays from additional mortgage purchases.

Housing for the Elderly (Section 202)

HUD recommends acceding to the will of the Congress, expressed in the 1976 HUD appropriations bill, by using the $375 million in Section 202 funds to provide permanent financing for elderly projects. The Labor-Management Committee has also recommended release of the funds for permanent financing. Secretary Hills believes her credibility is at stake on this issue.

OMB recommends deferring the 1976 funds until legislation can be enacted, allowing their use for construction financing only. Although OMB acknowledges that the chances for success are minimal, it believes the attempt should be made. Use of the funds for permanent financing would have almost no beneficial impact on the rents charged elderly tenants, but would require significant Treasury borrowing in each of the next 20 years. Since construction loans would be repaid in two years, the impact of such assistance on Treasury borrowing would be considerably less. OMB also recommends limiting the volume of loans to $215 million in 1977--the original 1975/1976 level (off-budget outlay savings - $24 million in 1978).

FHA Mortgage Insurance Program: Property Sales Targets

HUD recommends deemphasizing the technique of selling acquired property in as-is condition (that is, without major rehabilitation). As-is sales on a massive scale have been criticized by some mayors. Since the repair-and-sell approach is not able to move units out of HUD's inventory as quickly as the as-is approach, the Department recommends a reduction in the sales target approved in the budget for 1976, from 100,000 units to 73,000 units.

OMB recommends sales targets of 85,000 units in 1976 and 100,000 units in 1977 (outlay savings - $159 million in 1976 and $261 million in 1977). HUD acknowledges that the as-is approach is significantly more cost effective; public relations considerations account for the Department's recommendation. OMB argues that public relations considerations cut both ways; cities also desire to get unoccupied properties out of the HUD inventory and back into use quickly--something as-is sales can do much better than the time consuming repair-and-sell approach.

Rehabilitation Loans (Section 312)

HUD proposes to use the $50 million added to the 1976 budget by Congress for rehabilitation loans. The Department would not continue the program beyond its current expiration date of August 22, 1976.

OMB recommends seeking the rescission of all available funds (outlay savings - $53 million in 1976 and 1976 TQ). Financing private rehabilitation is an eligible activity under the Community Development Block Grant program, and in fact, recipients are using the funds to support rehabilitation as never before. The 312 loan program is merely another spigot for securing Federal dollars. Congress has already extended the program once, even though it was suppose to have been replaced by block grants. If these funds are not rescinded, the program is likely to gain momentum and be continued indefinitely.

Interest Subsidy Grants to State Housing Agencies (Section 802)

HUD recommends using the authority provided by Congress in the 1976 appropriation bill ($15 million annually for 40 years, or $600 million) on an experimental basis. The Department believes this would allow an increase in new construction under the

Section 8 rental housing program, and maintain the institutional capacity of some State agencies to administer Federal housing assistance.

OMB recommends that the full amount provided by Congress be proposed for rescission (outlay savings - $15 million in 1978). OMB believes Section 8 new construction should not be encouraged. In any case, grants under Section 802 are not required to facilitate borrowing by State housing agencies; full backing by their State governments would reduce interest rates below what Section 802 could achieve. Moreover, initiating the program--even on an experimental basis--would increase the demands for Federal guarantees under Section 802, which represent a much greater threat to the budget.

College Housing Direct Loans

HUD proposes to reopen the direct loan program on a one-shot basis in 1976 to take care of approved projects which cannot be completed with the Federal aid already provided. Once this has been done, HUD would propose rescission of whatever funds are leftover.

OMB believes the HUD proposal stands the best chance of avoiding an ongoing college housing program, which both agencies agree is not warranted. While all unused balances in this account could be removed without a rescission, thus avoiding the threat of an impoundment suit, such action would antagonize the Congress and prompt adverse legislation. Both HUD and OMB acknowledge, however, that the Congress might refuse to rescind the unused balances and thereby mandate an ongoing program.

Mobile Home Safety and Construction Standards

HUD recommends appropriations in 1976 ($1 million) and 1977 ($3 million) to get the mobile home enforcement program off the ground. The Department believes that use of Federal money at the outset would improve the chances for getting the States to take on the enforcement responsibility.

OMB recommends that fees rather than appropriated funds be used to launch the program (outlay savings - $3 million in 1977). In OMB's judgment, the States would be less inclined to take on the cost of enforcement if the Federal Government is already paying for it.

Fiscal Year 1977

Community Development Grants

HUD recommends the full amount authorized--$3,248 million--for block grants in 1977. Even with full funding, the program would be under great pressure since the amounts required under the statutory allocation formula are larger in 1977 than in either 1976 or 1978. HUD believes failure to request the maximum would prompt congressional action to extend hold-harmless or provide additional funds under the antecedent categorical programs (principally, urban renewal).

OMB concurs with the HUD recommendation. However, OMB estimates that outlays under the program will not occur as rapidly as HUD projects, and recommends reducing the budget estimates by $300 million (33 percent) in 1976 and $500 million (24 percent) in 1977.

Federal Housing Administration Mortgage Insurance Premiums

OMB recommends revising insurance premiums so as to put each program (including the recently reopened Section 235 program) on a sound actuarial basis, where existing law permits (outlay savings - $18 million in 1977 and $26 million in 1978). Most of the impact would be on the poor and minority groups who are the primary users of the unsound programs. On the other hand, there is no evidence to indicate that the in-kind subsidies provided through subsidized mortgage insurance produce benefits commensurate with the cost to the taxpayers.

HUD has determined what premiums are needed for actuarial soundness, and believes the impact on FHA insurance would be small (although some families could be priced out of the market). Even so, the Department does not recommend any premium changes until the issue can be studied further.

Rent Supplements

HUD requests an additional $30 million in contract authority ($1.2 billion in budget authority) which would be used to increase the Federal subsidy on existing rent supplement projects. The Department maintains that additional subsidies are needed to offset rising operating costs which could otherwise lead to defaults and subsequent insurance claims.

OMB recommends against requesting any additional contract authority in 1977 (outlay savings - $15 million in 1977 and $40 million in 1978). OMB believes that adopting a policy of meeting increased operating costs with increased Federal payments ("operating subsidies") would weaken the incentives for good management, and have serious consequences for the budget in future years.

Homeownership Counseling

HUD requests $6 million to launch a categorical counseling program for homeowners. The Department maintains that counseling is cost-effective, and failure to initiate a separate program is embarrassing politically.

OMB recommends against a separate counseling program (outlay savings - $3 million in 1977 and $6 million in 1978). HUD's own study of counseling indicates that it does not save the Federal Government money (as many in HUD argue). While counseling may be beneficial from society's standpoint, public and private agencies at the local level have both the incentive and capacity to underwrite it (as indeed they underwrite similar educational programs--driver's education, home economics, home repairs, etc.). A Federal program on the other hand, would establish a new group of social/welfare agencies dependent upon HUD for their continued existence.

Issue Papers

TAB C

1977 Budget
Department of Housing and Urban Development
Issue #1: Subsidized Housing

Statement of Issue

How many units of new and existing housing should be supported under HUD's subsidy programs in 1976 and 1977?

Background

- The 1976 Budget provided for approval of 400,000 units under the Section 8 rental housing program.

- The decision to reopen the Section 235 homeownership program anticipates approval for 130,000 units in both 1976 and 1977.

Alternatives

In addition to the 130,000 units to be approved under Section 235:

#1. Allow approval for 245,000 units under Section 8, none of which would involve new construction.

#2. Allow approval for 145,000 existing units under Section 8 and 100,000 newly constructed units under the Tandem Plan.

#3. Allow approval for 85,000 new and 160,000 existing units under Section 8 (OMB recommendation).

#4. Allow approval for 240,000 new and 160,000 existing units under Section 8 (HUD request).

Analysis

Obligations/Outlays ($ Millions)	1975 Ob.	1975 O	1976 Ob.	1976 O	TRQ Ob.	TRQ O	1977 Ob.	1977 O	1978 Ob.	1978 O	1979 Ob.	1979 O	1980 Ob.	1980 O	1981 Ob.	1981 O
Alt. #1	8,266	--	11,300	26	--	39	11,710	493	10,775	1,020	9,500	1,560	9,970	2,050	10,470	2,590
Alt. #2	8,266	--	9,950	26	--	31	9,790	465	7,280	1,060	6,020	1,520	6,300	1,810	6,600	2,140
Alt. #3	8,266	--	24,220	26	--	32	25,280	383	25,020	985	24,560	1,620	25,680	2,290	26,960	3,020
Alt. #4	8,266	--	32,975	26	--	32	55,475	383	56,720	1,340	57,740	2,400	60,630	3,710	63,660	5,120

Units (000's)	1975	1976	TRQ	1977	1978	1979	1980	1981
Alt. #1	92	375	--	375	318	245	245	245
Alt. #2	92	375	--	375	318	245	245	245
Alt. #3	92	375	--	375	318	245	245	245
Alt. #4	92	530	--	530	473	400	400	400

Employment (FTP's)	1975	1976	TRQ	1977	1978	1979	1980	1981
Alt. #1	N/A	893	892	905	226	262	298	334
Alt. #2	N/A	821	820	837	144	166	188	210
Alt. #3	N/A	1,121	1,120	1,298	622	661	700	739
Alt. #4	N/A	1,555	1,554	2,354	1,639	1,708	1,777	1,846

The principal points at issue are: (1) How many subsidized units should be approved in total? (2) What should be the mix between new construction and existing housing? (3) What program should be used to support new construction?

Number of Units

HUD and OMB agree that there is no programmatic basis for selecting any particular level of activity; the decision will be made on political and budgetary grounds.

. A 375,000-unit target (Alternatives #1 - #3) would be slightly below the 400,000-unit target adopted in the 1976 Budget.

. A 530,000-unit target (Alternative #4) would represent an unprecedented commitment to subsidized housing (the previous high was 427,000 in 1972).

New Construction Versus Existing Housing

The following table shows the lifetime cost of subsidizing a single unit under various programs (assuming rent levels increase 5 percent annually):

	Total Cost			Present Value		
	New Construction		Existing	New Construction		Existing
	Section 8	Tandem	Section 8	Section 8	Tandem	Section 8
Rent Subsidy.....................	$266,309	$ ---	$113,854	$ 71,472	$ ---	$29,943
Tandem Subsidy*..................	5,000	5,000	---	4,132	4,132	---
Total..........................	$271,309	$5,000	$113,854	$ 75,604	$4,132	$29,943
Total (rents increase 10%/year)	($861,288)	($5,000)	($367,806)	($211,098)	($4,132	($88,224)

* Not available at present for Section 8 units.

. Proponents of a new construction program point out that (1) 10 million households live in units that are too expensive, too small, or poorly equipped; and (2) the multi-family sector of the housing industry is producing at less than 50 percent of its equilibrium level.

. Opponents of a new construction program point out that (1) HUD's own study found housing deprivation to be an income, rather than a housing problem; and (2) with vacancy rates at an historical high, there is not a shortage of rental housing except where local rent control ordinances or fuel shortages have discouraged construction.

. The added cost of encouraging construction of a single unit under Section 8 (discounted present value) is:

	Rents Increase 5%	Rents Increase 10%
Subsidy Cost of New Construction..........	$75,604	$211,098
Less: Subsidy Cost of Existing Units.....	29,943	88,224
Cost of Construction Stimulus...........	$45,661	$122,874

. Existing units have a more immediate impact on the budget, but outlays on new units catch up by the third year.

Alternatives for Encouraging New Construction

. Clearly, the Tandem Plan represents a more cost-effective vehicle for encouraging new construction ($4,132 vs. $45,661 per unit).

. Suspending commitments for new units under Section 8 would be embarrassing to the Administration since this program has been heralded as the best means for promoting national housing goals.

HUD Request: Alternative #4, although the Department does not believe 240,000 new Section 8 units could be approved without Tandem subsidies, longer subsidy terms, and aid to State housing agencies. Secretary Hills has indicated to the Economic Policy Board that she would find Alternative #3 acceptable.

OMB Recommendation: Alternative #3. OMB believes that the volume of new construction supported under Section 8 should be kept as close to zero as politically possible, and in no case should additional sweeteners (such as Tandem subsidies) be extended to the program. Although OMB does not believe release of additional Tandem assistance for the multifamily housing sector is justified, we would recommend that in the event such a release is approved, it be accompanied by termination of Section 8's new construction component.

1977 Budget
Department of Housing and Urban Development
Issue #2: Mortgage Modification for Nonprofit Sponsors

Statement of Issue

Should HUD adopt a policy of restructuring mortgages on subsidized housing projects sponsored by nonprofit groups?

Alternatives

#1. Adopt a policy of restructuring mortgages on nonprofit-sponsored subsidized projects by deferring payment of (or writing down) up to 75 percent of total debt service requirements (HUD request).

#2. Continue the present ad hoc policy toward troubled projects.

#3. Adopt a policy of foreclosing on any assigned mortgage which cannot be made current after a specified period of time, and sell such projects with Section 8 commitments to protect the tenants (OMB recommendation).

Analysis

Budget Authority/Outlays* ($ Millions)	1975 BA/O	1976 BA/O	TRQ BA/O	1977 BA/O	1978 BA/O	1979 BA/O	1980 BA/O	1981 BA/O
Alt. #1:								
HUD estimate	--	+217	+114	+217	+87	+84	+64	+64
OMB estimate	--	+361	+184	+1,082	+1,250	+917	+632	+621
Alt. #2	--	--	--	--	--	--	--	--
Alt. #3	--	--	--	-118	-90	-90	-115	-110

* Change from the current policy (Alternative #2).

HUD and OMB disagree over how many projects would qualify for mortgage modification, and this disagreement accounts for the difference in outlay estimates under Alternative #1.

HUD estimates that 20 percent of all nonprofit-sponsored projects would be given relief. OMB believes that virtually all subsidized housing sponsors will seek relief from HUD, and the Department will be unable to prevent many of these sponsors from getting it. OMB's outlay estimates are based on the projection that 75 percent of all nonprofit sponsors and 33 percent of all limited dividend sponsors will qualify for modification.

HUD and OMB agree that the primary causes of defaults on insured multifamily mortgages are: (1) socio-economic factors which have prevented tenant income from keeping pace with rising operating costs, (2) poor underwriting by HUD that deliberately underestimated operating expenses to make projects appear feasible, and (3) poor management--especially where nonprofit sponsors are involved.

Alternative #1. HUD would defer up to 75 percent of the nonprofit sponsor's mortgage payments until the end of the mortgage term, provided (a) the sponsor had not intentionally defaulted, and (b) the project was not on a declining course. HUD acknowledges that "mortgage modification" is tantamount to writing down the mortgage, since the chances of the deferred amount ever being repaid are nil.

Advantages:

- Would postpone a congressionally mandated program of operating subsidies.
- Would remove the threat of legislation prohibiting foreclosures.
- Would avoid the political consequences of foreclosing on charitable groups.

Disadvantages:

- Would tighten HUD's link to the project, leaving the door open to operating subsidies in the future.
- Would maintain existing ownership which in many cases lacks both the ability to properly supervise management and the inclination to support management decisions.
- Would reduce incentives for sponsors to operate projects efficiently or remain current on their mortgages.

. Would have a significant and immediate impact on the budget since relief could be provided only after HUD has paid a claim equal to the outstanding balance of the mortgage on each project desiring Federal relief.

Alternative #2. Presently, HUD handles hopeless projects on a case-by-case basis. Hopeless projects sponsored by churches and other politically influential groups generally are kept in assignment indefinitely with what amounts to forbearance by HUD.

Advantages:

. Would have the same advantages as a writedown policy, since HUD--as lender--could forbear to the same extent it could write-down.

Disadvantages:

. Would have the same disadvantages as a writedown policy, except that the budget impact would be less (since an announced policy of leniency toward nonprofit sponsors would be more of a come-on than the present ad hoc policy).

. Would court congressional action, since the present policy does not give the appearance of a "permanent" solution to the nonprofit problem.

Alternative #3. HUD would foreclose on any project which could not be made current within a set period of time (say, 12 months). Foreclosed projects would be resold to the highest bidder, with provisions in the sales agreement earmarking Section 8 subsidies for existing tenants.

Advantages:

. Would end HUD's link to the project once and for all, thus removing the threat of further subsidies in the future.

. Would have a favorable impact on the sponsors' incentive to operate projects efficiently.

. Would have a favorable impact on the budget in the short run by discouraging defaults and increasing revenues from property disposition; to the extent the use of Section 8 subsidies does not increase the subsidized housing program level, the favorable impact would not be offset in later years.

Disadvantages:

- Would place an undesirable stigma on charitable groups, causing political problems.

- Would significantly increase the threat of congressionally mandated operating subsidies (which could be postponed by either of the other options).

- Would increase the threat of congressional action to prohibit foreclosures.

HUD Request: Alternative #1. The Department acknowledges that a foreclose-and-sell policy is considerably more cost effective. However, the Secretary believes that a mortgage modification policy is warranted in order to (1) maintain the existing stock of subsidized projects, and (2) forestall a congressionally mandated program of operating subsidies.

OMB Recommendation: Alternative #3. OMB does not believe mortgage modification can forestall Section 236 operating subsidies (although it might delay them for a few years). Experience under the public housing program (which involves the ultimate writedown--100 percent) indicates that capital subsidies are not enough to keep subsidized projects afloat.

OMB is continuing to explore the problem of multifamily defaults with HUD. In the event additional evidence to support Altenatives #1 or #2 is developed, the OMB recommendation might change.

Department of Housing and Urban Development
1977 Budget
Issue #3: Public Housing Operating Subsidies

Statement of Issue

Should rental charges in public housing be increased in order to reduce the need for Federal operating subsidies?

Background

. The median family income of public housing tenants on September 30, 1974, was $3,142, and the median family rent was $51 per month (19.4 percent of median family income; 22 percent of median family income less adjustments).

. In addition to paying for all construction/acquisition costs, HUD provides operating subsidies to local housing authorities (LHA's). Operating subsidies have risen from $12.6 million in 1969 to $475 million in 1975--an annual rate of increase exceeding 80 percent.

. A Performance Funding System (PFS) uses a set of objective standards to determine the level of operating subsidies going to LHA's. The standards apply only to operating expenses; LHA revenues are estimated using actual receipts in a base year, and a 3 percent inflation factor.

Alternatives

#1. Continue the performance funding system without change in 1977 (HUD request).

#2. Include a rent standard on the revenue side equal to 25 percent of adjusted income.

#3. Include a rent standard, and propose legislation eliminating deductions from gross income (OMB recommendation).

#4. Propose legislation that would phase out operating subsidies over a 10-year period.

Analysis

Budget Authority/Outlays ($ Millions)	1975 BA	1975 O	1976 BA	1976 O	TRQ BA	TRQ O	1977 BA	1977 O	1978 BA	1978 O	1979 BA	1979 O	1980 BA	1980 O	1981 BA	1981 O
Alt. #1 (HUD req.)	440	330	500	463	80	138	576	485	661	548	740	667	821	759	901	839
Alt. #2	440	330	500	463	80	138	497	462	580	474	656	583	735	674	812	752
Alt. #3 (OMB rec.)	440	330	500	463	80	138	410	437	490	395	564	489	640	581	714	657
Alt. #4	440	330	500	463	80	138	518	468	528	479	518	529	493	512	450	481

Increase in rent levels:	1975	1976	TRQ	1977	1978	1979	1980	1981
Alt. #1	---	---	---	+3%	+3%	+3%	+3%	+3%
Alt. #2	---	---	---	+14%	+3%	+3%	+3%	+3%
Alt. #3	---	---	---	+28%	+3%	+3%	+3%	+3%
Alt. #4	---	---	---	+13%	+14%	+14%	+15%	+15%

HUD and OMB agree that:

. Public housing projects have an enormous capacity to soak up Federal operating subsidies, and for this reason an objective, defensible method for determining an individual LHA's entitlement is essential.

. Public housing tenants (only 5 percent of the eligible population) are better off than comparable families outside public housing, since rents in these projects need not cover construction and financing costs.

Alternative #1 would not be controversial and, consequently, would do nothing to encourage adverse congressional action.

Alternative #2 would:

. Provide a more equitable means of allocating operating subsidies among LHA's.

. Encourage rent increases for some families, but still leave everyone at the 25 percent rent/income ratio that is considered acceptable for rental programs.

. Intensify political pressure on Congress to get rid of performance funding.

In addition to the effects listed under Alternative #2, Alternative #3 would:

. Increase rent for the typical family already at the 25-percent-of-income ceiling by $6.60/month (13 percent).

. Carry a much greater risk of congressional action, since new legislation would be required.

Alternative #4 would:

. Allow substantial savings in outlays and Federal employment (approximately 800 full-time permanent positions are budgeted for LHA-owned projects in 1977) over time.

. Impose a heavy burden on low-income families, even with a 10-year phase-in of rent increases (although these families would still be better off than comparable families outside public housing).

. Generate tenant unrest, rent strikes, and vandalism which could send some LHA's into bankruptcy.

. Have little chance of being approved by the Congress.

HUD Request: Alternative #1.

OMB Recommendation: Alternative #3. OMB believes that increases in rental charges are warranted from both a fiscal and equity standpoint, and would not impose an undue burden on public housing tenants.

Issue Paper
Department of Housing and Urban Development
1977 Budget
Issue #4: Comprehensive Planning Grants ("701")

Statement of Issue

What should be the funding level for the Comprehensive Planning (701) Program in 1977?

Background

- The Housing and Community Development Act of 1974 requires that, in order to be eligible for further comprehensive planning grants after August 22, 1977, each 701 applicant must have prepared housing assistance and land use plans.

- Community development block grants can fund all the planning activities currently funded by 701.

Alternatives

#1. Provide funding of $50 million for 1976 and 1977. This would require deferral of $25 million from 1976 to 1977 and new budget authority of $25 million in 1977 (HUD request).

#2. Release the full $75 million appropriation in 1976 and fold the program into the Community Development Block Grant Program in 1977 (OMB recommendation).

Analysis

Budget Authority/Outlays ($ Millions)	1975 BA	1975 O	1976 BA	1976 O	TRQ BA	TRQ O	1977 BA	1977 O	1978 BA	1978 O	1979 BA	1979 O	1980 BA	1980 O	1981 BA	1981 O
Alt. #1 (HUD req.)	100	97	75	112	0	29	25	40	50	50	50	50	50	50	50	50
Alt. #2 (OMB rec.)	100	97	75	117	0	34	0	43	0	7	0	0	0	0	0	0
(HUD original request before outlay reduction revision)	(100)	(97)	(75)	(117)	(0)	(34)	(100)	(63)	(100)	(97)	(100)	(100)	(100)	(100)	(100)	(100)

The 701 program is one of about 100 Federal planning assistance programs. Most of the other programs have narrower goals toward which planning is directed; 701 is unique in its wide flexibility. Numerous attempts have been made to consolidate or better coordinate these various programs, but with little success. The greatest obstacle to consolidating programs is delineating the recipients: Most funds do not go to State/local elected officials, but instead to State/local government agencies, planning districts, areawide bodies, water and sewer districts, river basin committees, etc. Consolidation of several programs would almost certainly require elimination of some of these recipients.

Arguments for continuing the 701 program:

- Areawide bodies, which comprise about 75 percent of the recipients of 701, are not eligible for community development grants.

- 701 May be credited with funding many State and local charter revisions and governmental reorganizations.

- 701 Provided an early impetus for States to undertake land use planning.

Arguments against continuing the 701 program:

- The community development grant program is of sufficient magnitude to easily replace 701.

- The original purpose of 701--to encourage hesitant local governments to undertake planning that would otherwise not be done--is outdated; local governments today possess the interest and the capability to undertake planning in areas they consider important.

- The 701 program, by heavily funding areawide bodies which are outside the political process, conflicts with a key Administration policy and the purpose behind the community development grant program--to direct funds to elected officials who will determine their use.

<u>HUD Request</u>: Alternative #1.

(1) 701 Funding is essential if regional planning activities providing for more organized growth in the future are to continue.

(2) 701 Is a potential coordinator and manager of other Federal planning activities: Operation of other planning programs by a single agency would be more efficient and could be absorbed within present personnel ceilings. This would result in savings to the Government in administrative costs.

OMB Recommendation: Alternative #2.

(1) All the activities funded by 701 may be funded by community development grants.

(2) There is no need to continue funding areawide bodies since local governments which comprise their membership could finance their activities. Further, it is of no benefit to the Federal Government to fund a planning effort, no matter what the national priority, if that plan will not be activated. If it is determined that an issue is timely or significant enough to warrant Federal funding, the assistance can be provided through community development grants and should be directed at those with the power to activate the plan--the State and local governments.