

Comment on James E. Wallace’s “The Dilemma of the Disposition of Troubled FHA-Insured Multifamily Rental Property”

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Introduction

In his article on U.S. Department of Housing and Urban Development (HUD) multifamily property disposition, James Wallace argues in support of relaxing the subsidy and affordability requirements governing HUD’s disposition activities for troubled developments. After presenting important data on the growing magnitude of this problem, Wallace correctly cites the obvious need for HUD to make improvements essential to reduce the problem’s scope in the near future, specifically in HUD’s practices for monitoring owners and avoiding default and foreclosure.¹ But when it comes to actual disposition policy, Wallace defends HUD’s currently proposed legislative retreat.

Wallace concludes that HUD should have more flexibility in determining what resources should be allocated to troubled properties and tenants, and he generally urges a “hold harmless” approach that would carry forward existing subsidies. Additional funds should be invested only as part of a comprehensive community revitalization plan. His rationale centers primarily on three points: (1) the lack of subsidy funds to meet current disposition requirements and the costs of HUD’s holding the properties; (2) the horizontal inequity of providing new subsidies to tenants of this housing in a “nonentitlement” environment; and (3) the nature of project-based subsidies, which can impede tenant mobility, contrary to HUD’s stated policy objectives. Along the way, Wallace makes some notable points about the growing need for affordable housing assistance and the irrationality of governmental accounting systems.

¹ That this need is obvious does not ensure that it will be addressed. Defining the specifics of an appropriate mortgage servicing policy to ensure quality housing and avoid defaults requires far more attention from HUD, owners, tenants and other advocates, and, possibly, Congress.

Wallace's article aptly poses the problem from an administrative and budgetary perspective. HUD faces additional staff reductions and competing demands for limited resources. Yet his analysis, like HUD's current proposal, is far too abstract. Neither his analysis nor his proposal adequately addresses how simply carrying forward existing or prior subsidies will solve the problems posed by these troubled housing developments. These developments are occupied predominantly by very low income people of color, are often in substandard condition, frequently have significant vacancy rates, and are affecting neighborhoods and communities around the country. Reducing new subsidy commitments will not resolve these problems or meet present or future residents' need for decent and affordable housing. Rather, Wallace's proposed solution, and HUD's, would transfer the problem to other parties and other levels of government without also transferring the plans, responsibility, and resources essential for real solutions.

True, HUD faces a growing disposition problem, as poor underwriting, lax mortgage servicing, mismanagement, and weak market conditions continue to increase default, assignment, and financial distress for developments with insurance still in force. But these serious problems did not develop overnight, nor are they caused by the current rules governing property disposition. These problems will not be solved simply by relaxing the subsidy requirements for property disposition. They will instead require structural reforms of the insurance programs and improved HUD monitoring and enforcement strategies, including more trained staff at the field level.

There is also a growing unmet need for affordable housing among families at or near the poverty level. Wallace uses this situation to support his claim that the disposition program distributes new assistance funds unfairly among those in need, since it confers benefits on current tenants or those who would occupy these rehabilitated units. However, an effective disposition program must address the physical, financial, and social problems of troubled developments. Therefore, the real task is to pursue targeting goals as much as possible while resolving the other issues that affect these developments and their communities.

What seems to underlie this recommended "cut and run" approach is an assumption that financial resources and HUD staffing levels and skills are both insufficient and immutable and that the federal government has no enduring responsibility to solve this problem. Under this view, HUD's policies must be

designed to fit within these “realities.” Housing policy, however, should be the product of a deliberative process that identifies goals and required minimum standards and then adapts the tools to fit those tasks. To begin the process otherwise leads to resources wandering in search of coherent objectives. This result we cannot afford, in either human or financial terms.

This comment argues that development of policy solutions requires better data about these properties, their occupancy, and the housing markets in which they exist. It also requires assignment of definitive responsibility to HUD for solving the problem. The policy should include some flexibility for HUD, communities, tenants, and purchasers to design appropriate solutions for particular developments, but it must define boundaries on the use of this discretion. These limitations should include certain guarantees for current tenants, adequate rehabilitation, and preservation of an appropriate portion of the units as affordable housing for very low income families, especially for those with worst-case needs. HUD must then request, and Congress must allocate, the resources necessary to accomplish these objectives.

The context of the dilemma

Wallace’s article provides some important information for understanding the property disposition issue. However, a more well-rounded picture of the problem and the issues presented is required for developing solutions.

Growing housing needs

Wallace demonstrates that we face growing needs for affordable housing assistance, especially among families with extremely low incomes. This phenomenon is essentially due to the fact that private-market low-rent units are disappearing and the incomes of the poor are not keeping pace with increases in housing costs. Incremental federally assisted units and subsidies have not kept pace with the growing need, with the result that we are falling further behind. Wallace’s point is that we obviously need to increase housing assistance for these families, but he questions whether attaching housing assistance to these HUD developments or providing it to these tenants is a wise and equitable use of federal housing funds.

While I believe that this society’s adoption of an entitlement to housing assistance—a “right to housing”—is a moral and social

imperative, this step would not wholly resolve the disposition dilemma.² A tenant-based entitlement would cure the problem of horizontal equity in subsidy allocation, but it would not ensure that these HUD developments receive either the resources or the stewardship sufficient to restore them to productive use. These properties need additional resources, not to expand housing assistance (although that purpose is a worthy one), but to make them viable assets for their residents and their communities.

Wallace contends that housing advocates have used the HUD disposition problem as a convenient justification for expanding subsidies in a nonentitlement environment. Certainly at times it may prove politically easier to obtain new housing assistance and meet growing housing needs by linking that effort to preserving existing developments. But this opportunistic characterization ignores the historical lesson that project-based subsidies are also usually essential for resolving the physical and financial problems of these developments, as explained below. Viewing the issue solely as one of the propriety of using this inventory as a vehicle for expanding assistance obscures the damage that would be caused by a “reform” that simply reduces additional subsidies.

The program and the properties

Program structure. Adequate consideration of property disposition policy and remedies requires some attention to the causes of the disposition problem. Multifamily developments default for many reasons, including poor underwriting, inappropriate risk allocation, mismanagement, market forces, and poor construction. But one of the key underlying causes of a project’s drift into troubled status and emergence as a disposition statistic is the flawed design of the insurance program. The federal government

² As other commentators have pointed out repeatedly, we already have an entitlement housing program for the wealthy, known as the mortgage interest and property tax deduction. This tax expenditure annually costs the government considerably more than the projected price tag for an entitlement program for worst-case very low income renters. Wallace estimates the cost of the latter at \$25 billion annually, whereas Follain, Ling, and McGill (1993) estimate the annual expenditure on the mortgage interest deduction alone at \$35 billion. Rectifying this glaring inconsistency is an important step on the road to housing justice. But since homeowners and industry trade groups will strongly resist relinquishing their entitlements, and since Congress will have a difficult time finding the money elsewhere to fund a worst-case program, we still need to figure out how to solve the problems of these HUD properties in an environment where funding for low-income housing assistance is limited.

takes the lion's share of the risk if the building fails, and the owner takes all the gain if it works. From the public's perspective, this is almost a "heads, you win; tails, we lose" situation. This structural flaw must be addressed through improved monitoring and mortgage servicing procedures, participation requirements, and disposition planning to ensure appropriate allocation of risks and responsibilities. These changes must be implemented with clear standards that will be monitored and enforced.

Program trends. Wallace provides important information about the downstream risks to HUD's portfolio indicated by various indices of stress and distress in these insured multifamily properties. This information underscores the need for HUD staff to implement early warning systems and adequate intervention policies; moreover, sufficient resources must be allocated in future years to deal with what are certain to be additions to the foreclosure and disposition pipeline. The data indicate that there will be no quick fix; instead, the problem demands a *comprehensive* policy and sustained administrative commitment.

The developments in question. Conspicuously lacking in the policy debate are any sound and consistent data on the developments and communities at issue. Wallace provides some gross data concerning tenant occupancy profiles and physical conditions drawn from a sample of properties surveyed for his recent HUD study. These data show that 90 percent of the tenants in the HUD-insured inventory have incomes less than the median. For troubled projects that are HUD-held or HUD-owned—the projects at issue here—it would not be surprising if the occupancy profile is far poorer, since these developments are in poorer condition, have higher vacancies, and consequently have lower rents than market alternatives. For older assisted projects, Wallace's data show that more than three-quarters of the tenants are very low income and almost all the remainder are low income. Again, for the subset of developments that have HUD-held mortgages or are HUD-owned, the figures are probably even higher.³ While Wallace's data show that most units are still of largely good quality, projects have significant capital needs that steadily increase.

HUD has been quick to share with Congress and the press its information on the growing scope of the problem: the numbers of projects and units broken down by program type (subsidized or unsubsidized), HUD region, and status (in foreclosure or

³ These are percentages of occupied units, and many troubled developments have very high vacancy rates.

HUD-owned) and annual trends and projections. These data have caused HUD to substantially increase loan loss reserves for the multifamily insurance fund, and HUD has used these data to move Congress to action.

The study conducted by Abt Associates for HUD and referenced in Wallace's article represents a good start in collecting much-needed information on multifamily properties with HUD-insured or HUD-held mortgages. However, to develop appropriate disposition strategies, we need even more data on troubled developments (including those owned by HUD) and the markets in which they exist, and the data must be used in developing and implementing policy. These data should be divided into developments with insurance in force, those with HUD-held mortgages, and those owned by HUD and should include the causes of the development's difficulties; vacancy rates; physical condition; occupancy profiles by income, family size, and race; location; and market rents now and after disposition. For each of these three property categories, we also need information on the specific HUD insurance or subsidy programs involved because current and pending legislation uses this information to allocate resources and protections. All this information is critical to projecting rehabilitation needs, operating income, and subsidy needs and to assessing the risks of displacement—all important factors in developing solutions. These variables bear not just upon affordable housing for current tenants and the larger community, but also upon project viability after disposition, a major concern of tenants, communities, and housing advocates.

The U.S. Government Accounting Office (GAO, unpublished data) has recently studied the characteristics of some of the HUD-owned inventory in Kansas City and Dallas. Although admittedly not a representative sample of the nationwide inventory, this information shows that almost 90 percent of tenants are very low income (especially in the formerly subsidized projects) and most are African American. These data also show that the properties are almost half vacant and have slightly below-market rents. Because such information has profound policy implications, HUD should immediately undertake efforts to collect similar data for a representative sample of the inventory of projects with mortgage insurance in force or with delinquent HUD-held mortgages, and HUD-owned projects. Only these data can yield accurate projections of resource requirements and support the development of necessary disposition tools.

Also needed is more information on how a property fits within the local housing market. What are the local needs for units with

project-based subsidies attached to make them affordable? What are trends in the local housing market, and what are the success rates for portable subsidy holders in finding adequate units? Should the development serve as a resource for meeting any unmet needs for project-based assistance? It is from these considerations that a comprehensive disposition policy should be developed, not from considerations of administrative convenience or simple deficit reduction.

The law, the policy, and the resources

Historical background of the current law and policy. Wallace recounts the development of the 1987 legislative requirements governing property disposition, but he characterizes them as new and driven primarily by the desire to expand housing assistance. Because they were neither, and because they are supported by other purposes, simply relaxing these requirements will not suffice.

Neither the timing nor the substance of the 1987 legislation was precise or sure to succeed, which is not unusual in the legislative process. The comprehensiveness and suitability of the 1987 Housing and Community Development Act's preservation remedies were complicated by the fact that HUD was not an effective or credible agent of congressional policy throughout the 1980s. In fact, HUD has not engaged in successful dialogues with Congress until very recently. Development of preservation policy is further complicated by the separation of the authorizing and appropriations functions within Congress; this separation sometimes leads to inconsistency between policy and resources. Now is an appropriate time to revisit the issues presented by the 1987 framework.

The 1987 act's requirements were not new. HUD itself created the Section 8 property disposition program in 1979.⁴ These rules required project-based Section 8 for all units in formerly subsidized projects and for those units in formerly unsubsidized projects serving as lower income housing resources. After the Reagan administration tried to repeal the rules through proposed regulations in the early 1980s and through legislation as recently as 1986, Congress codified them in the 1987 act. The 1987 act also extended similar requirements to units facing loss at foreclosure. Congress thus built on an existing program.

⁴ See HUD's property disposition program regulations adopted in 1979 (Office of the Federal Register 1979, 56609). Recently these regulations were significantly revised (Office of the Federal Register 1993, 43708).

Understanding this history is especially important, since in developing any new reforms Congress is likely to use many of these same tools rather than adopt a brand-new comprehensive approach. Although the disposition policy I outline later advocates a comprehensive approach, it is based on these existing tools.

The Section 8 requirement is important for reasons other than expanding assistance. Additional project-based subsidies are usually essential to resolving the physical and financial problems of these developments. Section 8 also promotes income mixing by allowing a spectrum of very low income households, including the working poor, to reside in these developments. Finally, project-based subsidies may be some families' only option for decent and affordable housing in markets where costs and discrimination are barriers to using tenant-based subsidies.

Thus, these 1987 statutory policies represented hardly a revolution, but simply a reaffirmation of then-current administrative policies.⁵ True, relaxing these requirements will mark the end of using the program to expand housing assistance, if that was ever its purpose, but it will not solve the dilemma.

The resources. Wallace correctly points out that HUD's inventory has increased dramatically because appropriations have been insufficient to operate the disposition program under the existing legislative requirements. For example, HUD's inventory of units owned grew from 10,000 to 27,000 between 1990 and 1992. What Wallace's data fail to tell us is the story behind the numbers: that this growth is largely due to deliberate choices. HUD, particularly during the Bush administration, chose not to request funding from Congress, and Congress chose not to appropriate the funds necessary to operate the disposition program.⁶ Over the same three-year period (1990 to 1992) that the

⁵ It should be emphasized that current policies do not require preservation subsidies for all troubled HUD-insured properties. Data from the GAO (1993) indicate that less than half (31,200 of 69,000) of the units that are in foreclosure or HUD-owned would require subsidies for preservation under current law. HUD field offices estimate that only 26,000 units, or not even 40 percent, require preservation.

⁶ During the early 1980s, Congress regularly appropriated sufficient funding to operate the property disposition program, typically ranging between 5,000 and 15,000 units of Section 8 subsidy annually; however, HUD often did not use all the funding appropriated. Appropriations began to decline in the mid-1980s, generally to about 3,000 to 5,000 units annually, reaching rock bottom in fiscal years 1992 and 1993 at 953 units annually.

HUD-owned inventory nearly tripled, appropriations for the program totaled fewer than 7,000 units.⁷

The point is this: During this period, had funding been requested and provided for more rational levels of property disposition,⁸ the problem of troubled properties would have been greatly mitigated, and it is likely that there would be no “crisis” today. In fact, even a meager appropriation of 5,000 units annually would probably have been sufficient to maintain the HUD-owned inventory at its 1990 level of 10,000 units.⁹ To a considerable degree, this crisis is the inexorable result of conscious funding choices, although such characterization makes resolving the crisis no less imperative.¹⁰

Furthermore, we must resist the temptation to view the current problem as insurmountable. In 1979, HUD owned 385 projects with approximately 40,000 units (U.S. House Committee on Government Operations 1983). It somehow managed to reduce its inventory to manageable levels under preservation requirements (the 1979 regulations) similar to the current statutory framework. Though many conditions are different today

⁷ Bear in mind that these subsidies had to cover not just sales from HUD’s own inventory, but also the preservation of those units purchased by an entity other than HUD at foreclosure. During this same period, a GAO (1993) report indicates that the Bush administration’s budget requests exceeded 21,000 subsidy units, a far more realistic figure. However, those requests were only for a five-year contract term with no insurance, which would not permit financing of needed repairs, so those requests were also inadequate.

⁸ A rational level would have been similar to the number of units requested by the Bush administration, which never exceeded 10,000 units annually. However, to permit financing of rehabilitation, the funding for that number of units would have had to include either 15-year contract authority or Federal Housing Administration mortgage insurance. Indeed, in the first years of the Reagan administration, funding was provided for about 10,000 units annually with 15-year contract authority.

⁹ This is because, of the 17,000 units added to the HUD-owned inventory between 1990 and 1992, an unknown but significant number are in formerly unsubsidized projects that do not require preservation under current law because they are either vacant or not occupied by low-income people. Of course, this estimate of the level of appropriations required to keep the HUD-owned inventory at its 1990 level does not consider another important aspect of the problem—the simultaneous growth in the number of properties in foreclosure or with delinquent HUD-held mortgages. Properties in these categories might eventually end up in HUD’s inventory.

¹⁰ The property disposition funding situation has improved of late. For fiscal year (FY) 1994, HUD requested and Congress appropriated funding for about 5,500 units of 15-year Section 8 authority.

(e.g., market conditions, tax laws), this history suggests that the current problem is solvable.

We must also resist the temptation to view HUD as incapable of providing solutions. Over the past decade it became fashionable to accept the characterization of HUD as inept, obstructionist, or incompetent. Though this premise was perhaps true in certain times and places, neither Congress nor HUD should ever base policy on it. An activist HUD committed to preservation can solve these problems, given leadership, staffing, a comprehensive policy, and adequate funding.

Current policy proposals

Wallace's prescription

Wallace makes the following proposals on disposition:

1. Generally withhold the attachment of additional subsidy funds to these properties by reforming the statutory mandates to permit flexibility while maintaining commitments to existing tenants and units.¹¹
2. Invest additional funds (including HOME funds) beyond the status quo only as part of a comprehensive community development plan.
3. Adopt or improve preventive measures designed to avoid default or foreclosure.
4. Reform federal budget accounting practices.

Wallace's reluctance to endorse additional subsidies for these developments, in an era when HUD resources lag behind growing needs, stems from two concerns: (1) Using funds in this way does not fairly allocate additional funds to currently unsubsidized households in proportion to their needs (the "horizontal equity" concern), and (2) attaching additional subsidies to properties in areas of high poverty or high minority concentration impedes tenant mobility, contrary to one of HUD's new initiatives. Since Wallace's ideas are similar to HUD's, I review them together below.

¹¹ To the extent additional subsidies are provided, Wallace advocates targeting those funds toward worst case households. Current preference rules for Section 8 assistance do provide for such targeting.

Pending House and Senate proposals

In the summer of 1993, HUD developed a legislative reform proposal that was introduced in the Senate as S. 1299 and characterized as Secretary Cisneros's top legislative priority. This proposal, which passed the Senate before adjournment in November, essentially mirrors Wallace's general recommendations. HUD's bill would generally require project-based subsidies upon disposition only for units that received such subsidies before foreclosure—a significant reduction from the requirements of current law.¹² HUD would impose rent restrictions on non-Section 8 units in formerly subsidized projects to provide below-market rents to tenants in some cases,¹³ but would require no restrictions on the non-Section 8 units in formerly *unsubsidized* projects, regardless of their occupants.

Even units that have or did have deep subsidies before foreclosure are not guaranteed project-based Section 8, since HUD's bill would permit the substitution of five-year tenant-based Section 8 in "soft markets" for some formerly subsidized units¹⁴ and would require that project-based Section 8 loan management subsidies for unsubsidized projects be converted to portable Section 8. HUD's bill would also permit other exceptions to carrying forward project-based Section 8 for "alternative uses" (e.g., non-rental use, mobility programs for people of color, neighborhood revitalization), limited to 15 percent of the disposition inventory. HUD's bill contains other elements, some of which are positive ideas.

Similar legislation was introduced in the House as part of a "reinventing government" proposal, H.R. 3400, which also passed

¹² Current law generally requires subsidies for all units in formerly subsidized projects and for those units occupied by lower income families in formerly unsubsidized projects.

¹³ For units rented to very low income tenants, rents would be limited to 30 percent of 50 percent of the area median income. For low-income tenants, the limit would be 30 percent of 80 percent of the median. In some cases these rent limits could produce a below-market rent, but in other situations actual market value of the units after disposition would be lower than these restrictions anyway. As with the HOME and tax credit programs, without additional subsidy, most tenants in the specified categories would not find these rents affordable, since by definition they are affordable only to families at the very top of each category.

¹⁴ Current law already allows such a substitution in soft markets for lower income units in formerly unsubsidized projects, and this would be maintained.

before adjournment.¹⁵ Although H.R. 3400 is in many respects similar to HUD's bill, HUD does not support the House version. One of the primary differences between the 1993 House and Senate bills, and the primary reason for the legislative impasse, is the House bill's attempt to provide rent increase protections for current tenants in an effort to avoid their displacement from rehabilitation and disposition. The House bill would limit rents for currently unassisted very low income tenants¹⁶ in formerly subsidized projects to 30 percent of their adjusted income. A similar restriction would be imposed for current very low income tenants of formerly unsubsidized projects, unless HUD finds that the restriction would "unreasonably impede" the disposition.¹⁷ The HUD bill would guarantee no protection for currently unassisted tenants beyond the flat rent restrictions required for formerly subsidized projects.

¹⁵ On February 10, 1994, Chairman Henry Gonzalez of the House Housing and Community Development Subcommittee introduced another piece of legislation on disposition as part of the HUD reauthorization bill (H.R. 3838) for FY 1995, which differs in several significant respects from H.R. 3400:

1. It eliminates the distinction between formerly subsidized and unsubsidized projects when allocating protections and resources.
2. It seeks to protect this stock as a resource for future low-income use by requiring certain occupancy and flat rent restrictions for all units that do not receive project-based Section 8 subsidies (with 40 percent of these non-Section 8 units reserved for very low income families at rents no more than 30 percent of 50 percent of median).
3. It requires affordable (30 percent of income) rent protections for all current very low income tenants, which in turn will usually require Section 8 subsidies.
4. It reduces the amount of stock unprotected through "alternative uses" to 5 percent.

The House may treat these provisions of this new bill as a substitute for H.R. 3400. Because they have not yet been introduced separately from the reauthorization bill, they are unlikely to receive more expeditious consideration that would permit an early conference with the Senate.

¹⁶ This generally means tenants of units that did not receive Section 8 before foreclosure.

¹⁷ In their current forms, these two bills cannot be sent to a conference committee because of Congress's procedural rules. To break the logjam, either the House must separately pass a property disposition bill or the Senate must pass a reinventing government bill. Alternatively, the issue may be addressed and resolved in the reauthorization process for FY 1995, scheduled for completion around the fall of 1994.

Shortcomings of current proposals and recommended policy directions

Default prevention policies and practices. Wallace's recounting of various suggestions for foreclosure avoidance contains several useful ideas, but they lack a key ingredient.¹⁸ Replicating a fundamental structural flaw in these programs, Wallace nowhere mentions basic tenant organizing and participation in project operation (outside the limited context of tenant ownership). Particularly in the face of increasing problems and concurrent proposals to reduce HUD staffing, others will have to perform the necessary day-to-day monitoring that HUD has historically proven incapable of providing.

Tenants are often perfectly situated to fulfill an important part of this role. For them to do so, however, requires assistance for basic organizing and training, as well as access to technical assistance for performing this function. This assistance must be provided within a policy framework that treats tenants as full partners in the program. Putting tenants first requires fundamental reorientation of HUD's loan servicing bureaucracy, but some current elements could be expanded (resident initiative specialists, training and technical assistance programs, and limited organizing grants for prepayment-eligible properties). This reorientation has an obvious link to overall efforts to reinvent government; to make HUD responsive to its beneficiaries; and to join housing assistance to jobs, social services, and economic and community development strategies. Such institutional reform could improve housing quality and living environments in a way that could outlast any one secretary's policies.

An effective prevention program to reduce deterioration, defaults, and foreclosures must also reform HUD's predefault mortgage servicing policies and practices, the servicing and workout policies for HUD-held mortgages, and HUD's performance as mortgagee in possession or owner. All these reforms have significant short- and long-term financial consequences.

Revised federal accounting practices. Wallace's point about the irrationality of federal budget accounting practices concerning mandatory and discretionary spending is well taken. In its FY 1995 budget, HUD has proposed to shift much of the property disposition cost to the mandatory side, to be offset by savings in maintenance and holding costs. This would be a logical step, but

¹⁸ The House and Senate bills leave resolution of these issues to HUD's internal administrative reforms, at least for the moment.

political support from the Office of Management and Budget and Congress may prove elusive.

Disposition policy. Any new disposition policy and resources must resolve the problems created by these properties and by the federal government's creation and administration of these programs. Simultaneously, it must protect current tenants against displacement. Neither HUD's bill nor Wallace's proposal accomplishes these tasks.

Under the guise of "sensible retrenchment," Wallace and HUD would dump these problem properties onto local communities without providing adequate resources to deal with them. This approach only compounds the problem and leaves no one responsible for its solution. HUD has a legal and moral responsibility to these complexes, these tenants, and their neighborhoods to resolve the problem of troubled properties in a way that furthers the national housing goal of "a decent home and suitable living environment for every American family" (as stated in the preamble to the Housing Act of 1949).

Wallace's proposal and HUD's bill (S. 1299), born primarily of concerns for administrative flexibility and financial expediency, fail to set sensible goals and ensure certain essential protections for both tenants and the housing. While it may not be possible or desirable to preserve all units as affordable housing and provide truly affordable rents for all tenants, the question is which units and tenants should be addressed, and how. While administrative and financial objectives are important considerations in overall policy design, they ought not dominate to the exclusion of the needs of residents, developments, and neighborhoods. Such limited motivations will harm many very low income tenants, and the physical, management, and financial problems of much of the multifamily stock will not be solved, posing continuing hazards for neighborhoods and communities. A coherent policy conferring basic minimum protections is even more critical should the discretionary decision making advocated by Wallace and HUD pass to an administration that does not share previously articulated policy objectives.

Wallace's and HUD's reliance on the subsidy situation before foreclosure (holding tenants harmless) as the appropriate benchmark incorrectly assumes that the status quo ante provided sufficient resources for repair and operation of these developments or that a simple acquisition debt write-down through a purchase price discount for a new owner can fill any gap. In reality, additional project-based subsidies, in conjunction with

competent ownership and management, will be essential to resolving the physical and financial problems of many of these developments, given their occupancy profile, market location, and rehabilitation needs. Section 8, or a comparable subsidy to make rents affordable, is also needed to permit a cross section of very low income families to reside in a viable development.

Nor does maintaining prior Section 8 levels hold all tenants harmless, since other tenants could see significant rent increases from rehabilitation and disposition. Even imposition of flat rents on non-Section 8 units in formerly subsidized developments, as proposed in the HUD bill, will guarantee affordability only for those at the top of the low or very low income categories.

Regardless of the horizontal equity and mobility concerns raised by Wallace, use of this HUD multifamily stock as a resource for providing housing assistance is inevitable if the current problem is to be resolved. Troubled developments must be restored to viable use, and very low income tenants in need of assistance often live in these developments. Since these tenants cannot afford the restoration costs, significant subsidies will be required for previously unassisted families. At the same time, if a commitment of additional federal resources is required, care must be taken, as Wallace suggests, to ensure that an appropriate share of these new resources benefits those very low income families most in need of housing assistance. Otherwise, preservation could divert substantial federal resources to families without worst-case needs.

Coordinating new disposition investments with community revitalization efforts makes sense, since local government and neighborhood contributions will be important parts of many turnaround strategies. However, establishing local support as a prerequisite to additional federal resources, as Wallace suggests, would be unwise. One of the unstated premises of such a linkage is that the development itself cannot be successfully restored without such broader planning, which may be untrue. The linkage also assumes that governments share a desire to resolve these problems. Without specific federal requirements that condition receipt of other funds that a community might want (perhaps Community Development Block Grants or, to a lesser extent, HOME) on the creation of an adequate plan, many local governments will be content to focus their attention elsewhere. The linked federal resources suggested by Wallace are a carrot that will often go uneaten, and properties and neighborhoods will continue to suffer.

One also cannot consider preservation policy for these properties without analyzing the fair housing implications. Regardless of HUD's or Wallace's policy preference for mobility approaches,¹⁹ Congress should ensure that tenants and communities are consulted about the desirability of any such policy, since their homes and communities are at stake. In many cases, the tenants of these units are predominantly minority. Often the developments contain larger units that are desperately needed by families with children. Given the barriers to use of the private market, without substantial support resources it may often be very difficult to provide housing opportunities for these families through any method besides a comprehensive preservation strategy. Subject to the approval of those families affected, this strategy could use subsidies for formerly unsubsidized units in largely white or integrated census tracts.

Cost is an important consideration in developing any new policy. Wallace lists (in his table 6) estimated five-year costs of \$5.4 billion, \$3.6 billion, and \$1.8 billion under the requirements of current law, HUD's bill, and last year's five-year Clinton budget, respectively. What remains unclear is whether HUD's proposed \$3.6 billion would be adequate to solve the problems presented while protecting tenants. HUD does not know the answer because it does not have the right data on these developments, their markets, and their tenants. Without such data, no one can accurately project needs and costs or determine what tradeoffs are required, either by reallocating resources from elsewhere in HUD's budget or by compromising some of the principles detailed below.

An alternative policy approach

A sound policy should contain at least the following elements and basic protections, for *both* developments facing foreclosure and those being sold from the HUD-owned inventory. These elements are not inherently inconsistent with the greater flexibility that HUD seeks; they are insurance against permitting such flexibility and discretion alone to pass as responsible

¹⁹ Encouraging tenant mobility was called "deconcentration" in S. 1299. The term itself is objectionable because it implies that there is something wrong with poor or minority households choosing to remain in a community if that community has a predominance of poor and minority people and with federal policies that provide assistance to support that choice. While mobility remedies may be helpful for some families, they will rarely alleviate the problems of racism and poverty for all these residents and their communities.

housing policy in times of limited resources. They center on the ingredients for protecting tenants and ensuring successful developments.

1. Sound comprehensive disposition planning that includes a specified role for tenants (with the organizing and technical assistance resources to make it meaningful), the community, and the local government
2. An adequate and financially feasible rehabilitation plan, with the necessary standards and resources to ensure the long-term physical integrity and habitability of the complex²⁰
3. Competent ownership and responsive management, maximizing tenant and nonprofit control where appropriate²¹
4. No displacement of existing residents as a result of the economic consequences of disposition and rehabilitation, which at least requires protection against rent increases
5. Affordable rents for all units occupied by low and very low income families (no more than 30 percent of adjusted income)
6. Maximum targeting of units for a wide range of very low income families, consistent with available resources and economic mix goals
7. Long-term “useful life” use restrictions for any developments receiving more federal resources
8. Public and tenant monitoring and enforcement of disposition plans and of clear maintenance, management, and operational standards (to avoid a vacuum of oversight and

²⁰ This plan should include linking new federal investments with requirements to improve economic opportunities for residents of the development and the neighborhood to the maximum extent feasible.

²¹ Both the repair and competent ownership/management goals are very difficult to achieve in the context of a foreclosure sale in which the project is sold to the high bidder as long as certain minimal requirements are met. Because overall disposition planning is much more workable when projects are sold from the HUD inventory (as opposed to a foreclosure sale), any reform should specifically require the agency to bid the project’s entire debt plus any advances, to maximize the chances of HUD becoming owner and to maximize its ability to formulate sound disposition plans. HUD will undoubtedly strongly resist accepting this responsibility.

accountability, HUD must remain clearly obligated to play an enforcement role regarding these buildings unless that duty is delegated to other qualified public agencies)

9. Adequate financial resources in the form of mortgage insurance, grants, subsidies, or acquisition debt reduction to permit long-term, cost-effective solutions
10. Adequate HUD staffing and skills to implement these objectives

Some of these elements, and other important features, although absent from HUD's initial proposal as introduced, have already been addressed by one or both of the Senate and House bills as passed.²² Others remain lacking or in need of significant improvement. For example, the bills do not clearly require disposition planning and protections at the point of foreclosure. Since the point of sale is irrelevant to the needs of the tenants or the housing, coverage to the greatest extent legally possible is important, especially in light of HUD's preference for disposing of buildings through foreclosure.

So far, neither bill seems likely to require an improved insurance program or other tools to maintain adequate federal oversight of these properties. Requiring HUD to provide insurance would ensure greater incentive for the federal government to assume sufficient responsibility not just to process sales, but also to ensure successful future operations.²³ It would also reduce the Section 8 budget authority needed for 5-year contracts (rather than the 15 required for private financing).

Congress will undoubtedly be considering these issues as the pending legislation or the FY 1995 reauthorization proposals move forward. Wallace's article provides a useful contribution to this debate. Resolving the dilemma itself will require more information from HUD and principled scrutiny from Congress.

²² These include (1) comprehensive disposition planning, involving the tenants and the affected communities; (2) an authorization for technical assistance for residents and prospective purchasers; (3) opportunities for tenant and non-profit purchase; (4) long-term use restrictions for properties receiving significant federal benefits; (5) tenant participation in alternative use decisions; and (6) replacement tenant-based subsidies and HUD-mandated support services to ensure housing for tenants involuntarily displaced by HUD decisions.

²³ Of course, servicing reforms would have to be instituted simultaneously to avoid replication of the current situation.

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