

August 1998

SECTION 8 HOUSING ASSISTANCE

HUD to Recapture \$439 Million of Excess Funding in the Moderate Rehabilitation Program



**Resources, Community, and
Economic Development Division**

B-280439

August 25, 1998

Congressional Committees

The Department of Housing and Urban Development's (HUD) Section 8 Assisted Housing Program provides rental subsidies for low-income families. Assistance is either tenant-based assistance (linked to specific households) or project-based assistance (linked to specific housing units). The Section 8 Moderate Rehabilitation (MOD REHAB) Program is a form of project-based assistance administered by state and local housing agencies under contract with HUD. It was created to upgrade substandard privately owned rental housing requiring a moderate level of rehabilitation.

As the Chairman of the Subcommittee on VA, HUD, and Independent Agencies, House Committee on Appropriations, you asked us to review HUD's financial management of the Section 8 Program. In response to that request and to a mandate in the 1997 Emergency Supplemental Appropriations Act (P.L. 105-18) that directed us to review HUD's budgeting and accounting systems for Section 8 rental assistance, we agreed to issue three reports on HUD's financial management of the Section 8 Program, focusing on tenant-based assistance, project-based assistance not including the MOD REHAB Program, and the MOD REHAB Program. Reports we issued on tenant-based and project-based assistance in February 1998 and July 1998, respectively,¹ focused on identifying excess budget authority and HUD's efforts to recapture those funds.² The Congress has rescinded several billion dollars of excess budget authority that had been appropriated for Section 8 assistance in prior years.

In this report, the third in the series, we provide information on (1) the amount of excess budget authority in the Section 8 MOD REHAB Program and how HUD estimated this amount; (2) the accuracy of HUD's estimate; and (3) HUD's plans for recapturing, or taking back, this excess budget authority from housing agencies.³ We relied on information provided to us from the information system that HUD uses to manage the MOD REHAB

¹Section 8 Tenant-Based Housing Assistance: Opportunities to Improve HUD's Financial Management (GAO/RCED-98-47, Feb. 20, 1998) and Section 8 Project-Based Rental Assistance: HUD's Processes for Evaluating and Using Unexpended Balances Are Ineffective (GAO/RCED-98-202, July 22, 1998).

²To recapture funds, HUD first identifies and confirms the amount of excess budget authority that it has obligated to a housing agency and then deobligates the funds, or takes the funds back from the agency, by making the appropriate changes to the accounting system.

³This report does not discuss one segment of the Section 8 MOD REHAB Program—the Single Room Occupancy Program—because it is administered separately from the rest of the program and, therefore, not included in HUD's analysis of excess budget authority.

Program and from officials in HUD's offices of Public and Indian Housing and the Chief Financial Officer.⁴

Results in Brief

In January 1998, HUD estimated that the amount of excess budget authority in the Section 8 Moderate Rehabilitation Program before necessary adjustments was \$814 million; after subtracting amounts required to cover future requirements and contingencies, HUD estimated that \$439 million could be recaptured—that is, taken back—from the housing agencies that the Department contracts with to administer the program. HUD estimated these amounts after first addressing certain known problems with the data in its information system and then comparing the level of unspent program funds at each participating housing agency with that agency's future need for funding under its current contract with HUD.

We cannot determine the accuracy of HUD's estimate of excess budget authority in the Section 8 Moderate Rehabilitation Program at this time because HUD has neither completed identifying and correcting discrepancies in its data on the program nor tested the reliability of the data it used to estimate the excess budget authority. Because HUD still is not confident that its program data are sufficiently accurate, the Department plans to require its field staff to identify and address discrepancies in the accuracy of contract data and to work with a contractor to further address the data's problems on-site at housing agencies. HUD officials do not expect these data cleanup efforts to be completed before the end of fiscal year 1998. In addition, HUD plans to require its contractor to perform a statistically valid test of the accuracy of its information system.

Although HUD plans to recapture the excess budget authority in the Section 8 Moderate Rehabilitation Program, the Department has not finalized its approach or time frame to accomplish this task. In addition to completing the planned data cleanup efforts in the field, HUD must also develop and test the formula it will use to recapture the excess budget authority from the housing agencies' accounts. While some factors in the formula are not within HUD's discretion to change, policy decisions still need to be made to define other factors. For example, after completing data cleanup efforts in the field, HUD may decide that it does not need to leave as much excess budget authority in the housing agencies' accounts to cover contingencies as it originally had estimated in January 1998. Therefore, the actual

⁴HUD's Central Accounting and Program System, called HUDCAPS, provides accounting and program management capabilities for the Section 8 tenant-based and MOD REHAB programs.

amount recaptured from housing agencies and available for rescission by the Congress may change and perhaps be more than the \$439 million estimated in HUD's January 1998 analysis. HUD officials could not provide us with a firm estimate of when the Department will finalize its recapture plan and could not predict a date for completing the recapture.

Background

HUD's Section 8 Assisted Housing Program provides rental subsidies for low-income households. Assistance is either tenant-based—the household receives the assistance wherever it finds an acceptable housing unit owned by a landlord who agrees to participate in the program—or project-based—rent is paid for an eligible tenant or tenants when they occupy a specific housing development or unit. For tenant-based assistance, HUD contracts with and provides funding to local and state housing agencies to administer the program. In turn, these agencies make payments to private sector landlords to subsidize the rent for eligible households. For most project-based assistance other than the MOD REHAB Program, HUD contracts directly with and provides rental subsidies to the owners of private rental housing and to state finance agencies. Although the MOD REHAB Program is a type of project-based assistance, it is administered by local housing agencies under contract with HUD. For each type of Section 8 housing assistance, participating households generally pay 30 percent of their income for rent, although this percentage can vary depending on family income and program type.

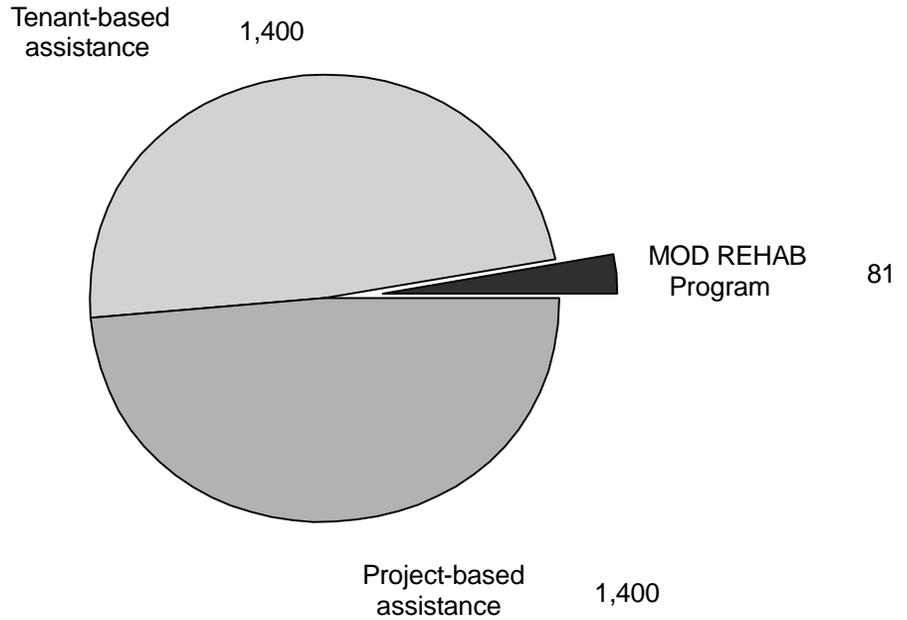
The Section 8 MOD REHAB Program was created in 1978 to add to the existing inventory of assisted housing. It did this by providing funding to upgrade a portion of the estimated 2.7 million then-unassisted rental housing units with deficiencies that required a moderate level of repair and rental subsidies for low-income families. Under annual contracts with housing agencies, HUD provides the funding for rental subsidies as well as an administrative fee to the agencies. The administering agencies, in turn, enter into Housing Assistance Payments (HAP) contracts with property owners. Under these HAP contracts, property owners rehabilitate their housing units by completing repairs costing at least \$1,000 so their units meet HUD's standards for housing quality and make the rehabilitated units available to eligible families. In exchange, the housing agencies screen applicants for eligibility and pay the difference between the approved contract rent and the tenants' portion of the rent. Initially, the contract rent is based on an owner's costs, and housing agencies can approve rents up to 120 percent of an area's fair market rent to compensate the owner for rehabilitation costs. However, when the term of a property owner's

rehabilitation loan is less than the term of a HAP contract, regulations require housing agencies to adjust the contract rent downward at the end of the rehabilitation loan's term to reflect the owner's reduced expenses.

During the 11 years that the Congress funded new contracts under the MOD REHAB Program,⁵ the term for HAP contracts was 15 years. When the oldest of these contracts began to expire in 1995 and 1996, HUD instructed housing agencies to replace them with Section 8 tenant-based assistance. Since fiscal year 1997, however, the Congress has required HUD to renew an expiring contract with a 1-year MOD REHAB contract if the owner so requests and the property consists of more than four housing units covered in whole or in part by a HAP contract. In calendar year 1997, about 25 percent of these expiring HAP contracts were renewed as 1-year MOD REHAB contracts. As of January 15, 1998, the MOD REHAB Program was assisting over 81,000 households, but this represents a small proportion of the total number of households receiving Section 8 assistance (see fig. 1).

⁵The Congress has not funded new MOD REHAB contracts since 1989. After amending the MOD REHAB Program in 1989 to require, among other things, that the minimum expenditure per unit be \$3,000, the Congress repealed the program in 1990.

Figure 1: Number of Households Receiving Assistance Through the Section 8 Program, Households in Thousands



Source: The figures for tenant-based, project-based, and MOD REHAB assistance are from data analyses performed by HUD in February 1997, June 1997, and January 1998, respectively.

The excess budget authority in the Section 8 MOD REHAB Program is funding that has been obligated to the housing agencies that administer the program but will not be needed to meet the agencies' obligations under current contracts. Three types of such funding exist in the Section 8 MOD REHAB Program: (1) funding that has been obligated to a housing agency but never been placed under a HAP contract, (2) budget authority that has been placed under a HAP contract but has not been used and thus has accumulated in a housing agency's reserve account,⁶ and (3) excess funding that HUD estimates will accrue in a housing agency's reserve account. The third type of excess budget authority cannot be recaptured until it actually accumulates in a housing agency's reserve account. HUDCAPS is designed to capture the data necessary to calculate the total amount of excess budget authority that has accumulated in the program

⁶Each year, an amount of budget authority equal to the difference, if any, between the total amount authorized under a housing agency's contract with HUD and the housing agency's actual payments under HAP contracts with property owners is credited to the housing agency's reserve account. The portion of these reserves that the housing agency will not need to meet current contract requirements is excess budget authority.

on an annual cycle as each housing agency reports its actual program costs to HUD.

Comparing Unexpended Budget Authority With Future Needs for Each Housing Agency Has Yielded an Estimated Excess of \$439 Million

In January 1998, HUD estimated that the excess budget authority in the Section 8 MOD REHAB Program was \$814 million before adjustments. After subtracting amounts required to cover future requirements and contingencies, HUD estimated that \$439 million could be recaptured from the housing agencies that administer the program. HUD did not recapture the excess budget authority in the MOD REHAB Program in September 1997, when it recaptured similar excesses in its tenant-based program because, according to HUD program officials, the Secretary of HUD did not have the authority to do so. In addition, problems with its data on the MOD REHAB Program would have made it difficult for the Department to identify and recapture excess budget authority. For example, some HAP contracts had not been entered into HUD's information system, and some of the data on the number of units under contract had been entered incorrectly. Therefore, HUD instructed its field offices to address these discrepancies by comparing the data in its central information system with the data in the Department's original contracts with housing agencies and the original HAP contracts and then making any necessary changes. Although this internal effort to correct the data ended in December 1997, HUD officials believe that the accuracy of the data could be further improved and that approximately 10 percent of the system's entries are inaccurate. As discussed later, HUD plans additional efforts to correct its data.

After updating its information system to reflect the December 1997 corrections, the Department analyzed the system's data to estimate the amount of MOD REHAB excess budget authority that was available for recapture and reuse. To estimate this amount, HUD first calculated the excess budget authority by comparing the total unexpended budget authority with the program's requirements for that budget authority at each housing agency—the same method that it had used to determine the excess budget authority in its tenant-based program. As shown in table 1, HUD then determined that the total excess budget authority available as of January 15, 1998, was about \$814 million before adjustments. Of that amount, HUD estimated that it would need about

- \$191 million to cover known funding shortfalls for HAP contracts that have not had sufficient funding obligated to them to cover their expected needs

through the end of their terms and

- \$184 million to cover such contingencies as unexpected decreases in tenants' incomes or unexpected rent increases.

According to HUD, the remaining \$439 million is available for recapture and reuse to meet ongoing needs for housing assistance. The Congress may also decide to rescind this excess budget authority as it did when excess budget authority was identified in the Section 8 tenant-based program.

Table 1: Excess Budget Authority Available for Recapture and Reuse

Dollars in millions	
Excess budget authority available as of January 15, 1998 (before adjustments)	\$814
Less: Amount of adjustment to cover known funding shortfalls in the program	(191)
Less: Amount of adjustment to cover contingencies	(184)
Excess budget authority available for recapture and reuse	\$439

Source: HUD's Office of Public and Indian Housing.

The \$184 million reserve for contingencies is equivalent to almost 4 months of housing assistance payments to property owners participating in the MOD REHAB Program. When HUD recaptured the excess budget authority in the Section 8 tenant-based program in September 1997, the Department held in reserve for contingencies an amount equal to only about 2 months of housing assistance payments to property owners. According to HUD officials, the Department established a larger reserve for contingencies in the MOD REHAB Program than the one it had established for the tenant-based program because, at the time the analysis was performed, it did not have as much confidence in its data for the MOD REHAB Program as it did in its data for the tenant-based program.

The Accuracy of HUD's Estimate Cannot Be Determined Without Evidence of Reliable Data

We cannot evaluate the accuracy of HUD's estimate at this time because the Department has not completed its efforts to reconcile discrepancies between the data in its information system and contract documentation contained in field offices' files. Despite HUD's earlier efforts to improve its data on the MOD REHAB Program, the Department was not able to correct all the discrepancies identified before performing its analysis of excess budget authority. For example, at the time HUD performed its analysis, some HAP records still were incomplete and others contained irregular

data. At the time of our review, officials in the Office of Public and Indian Housing qualitatively estimated that HUD's data on the MOD REHAB Program were not entirely accurate in terms of being correct and complete. To further improve the data's accuracy, HUD plans to continue correcting discrepancies in contracts that it has with housing agencies. HUD also plans to obtain an independent and statistically valid evaluation of the accuracy of the data in the MOD REHAB Program's information system.

HUD recognizes that its data on the MOD REHAB Program are questionable; therefore, it plans to undertake additional efforts to verify the information. First, HUD plans to instruct the staff in its field offices to again compare the MOD REHAB data in its information system with the data contained in the original contract documentation maintained at those offices. HUD officials explained that potential data inconsistencies will be reported to its field offices, which will reconcile the data by using the information in their contract files. However, because it believes that the documentation at its field offices will not always be reliable, HUD also plans to hire a contractor to follow up on and correct discrepancies by obtaining missing or additional information from the housing agencies that administer the program. By taking these steps, HUD hopes to enhance the integrity of its data on the MOD REHAB Program. The Department expects its field offices to complete their portion of the data reconciliation by the end of August and the contractor to complete the rest of the data retrieval by the middle of October.

For its Section 8 tenant-based program, HUD engaged a contractor to independently evaluate its estimate of excess budget authority. The contractor also conducted a representative sampling of transactions in its information system and developed a statistically valid estimate of the system's accuracy. HUD plans to require the contractor that will be correcting contract discrepancies to perform a similar evaluation of the accuracy of the MOD REHAB Program's information system. Until HUD completes such an evaluation, we cannot report on the accuracy of HUD's estimate of its excess budget authority.

HUD Has Not Finalized Its Plans to Recapture the Excess Budget Authority in Its Mod Rehab Program

Although HUD plans to recapture the available excess budget authority from housing agencies' accounts, the Department has not finalized its plans for this activity, according to officials in HUD's offices of Public and Indian Housing and the Chief Financial Officer. For example, in addition to completing the data cleanup efforts discussed above, HUD also needs to develop and test the formula it will use to recapture the excess budget authority from housing agencies' accounts. While some factors in the formula, such as the inflation rate and certain economic assumptions prescribed by the Office of Management and Budget, are not within HUD's discretion to change, other aspects of the formula are still undetermined. For example, HUD may decide after its field offices complete their efforts to clean up the data that it no longer needs to keep the full \$184 million in the housing agencies' accounts to cover contingencies, as it originally had estimated in January 1998. This means that the actual amount recaptured and available for rescission may change and perhaps be more than the \$439 million estimated in HUD's January 1998 analysis.

HUD officials could not provide us with a firm estimate of when the Department will finalize its recapture plan and could not predict a date for completing the recapture.

Conclusions

Once HUD identifies the amount of excess budget authority in its Section 8 Program, the Congress has shown that it will act expeditiously to make the most productive use of that authority. Therefore, we believe that HUD is correct in taking steps to identify and plan for recapturing the excess budget authority in its MOD REHAB Program. Identifying, confirming, and recapturing this excess budget authority before HUD submits its fiscal year 2000 budget request would help to show that HUD is making progress toward improving its financial management of the Section 8 Program. To do this, HUD will need to complete its work to clean up its data, evaluate the accuracy of its data, and develop its recapture formula as soon as possible.

Because HUD recognizes the steps it needs to take to properly report to the Congress the amount of excess budget authority in its MOD REHAB Program and has plans to take such steps, we are not making recommendations at this time. However, we will continue to monitor HUD's budget process and review its fiscal year 2000 budget submission to determine whether the Department's cost estimates accurately reflect the amount of its excess budget authority.

Agency Comments

We provided a draft of this report to HUD for review and comment. In commenting on the report, HUD said that it generally agreed with our assessment of the steps being taken to properly report to the Congress the amount of excess budget authority in the Section 8 MOD REHAB Program. The Department also provided several technical comments, which we incorporated, as appropriate. HUD's letter appears in appendix I.

Scope and Methodology

To determine how HUD estimated the excess budget authority in its Section 8 MOD REHAB Program and the accuracy of this estimate, we discussed with Department officials their general approach for calculating excess budget authority and reviewed preliminary documentation supporting their approach. Specifically, we discussed HUD's approach with officials in the offices of Public and Indian Housing and the Chief Financial Officer and analyzed reports from HUD's accounting system that showed the amount of excess budget authority available for recapture from the housing agencies that administer the program. However, at the time we completed our review, HUD had not finalized its recapture plan and the assumptions that will determine the specific amounts to be recaptured from each housing agency. To determine what HUD plans to do with the excess budget authority in the Section 8 MOD REHAB Program, we interviewed program and budget officials and officials in HUD's Office of the General Counsel about the Department's plans and legal authority to recapture the program's excess budget authority and reuse it to meet ongoing needs for housing assistance. We performed our work from February 1998 to July 1998 in accordance with generally accepted government auditing standards.

We are sending copies of this report to the appropriate House and Senate committees; the Secretary of Housing and Urban Development; and to the Director, Office of Management and Budget. We also will provide copies to others on request.

If you or your staff have any questions concerning this report, please contact me at (202) 512-7631. Major contributors to this report were Eric Marts, Assistant Director, and Paige Smith, Senior Evaluator, of our Resources, Community, and Economic Development Division.

A handwritten signature in black ink that reads "Judy A. England-Joseph". The signature is written in a cursive style with a large initial 'J' and 'A'.

Judy A. England-Joseph
Director, Housing and Community
Development Issues

List of Congressional Committees

The Honorable Christopher S. Bond
Chairman

The Honorable Barbara A. Mikulski
Ranking Minority Member
Subcommittee on VA, HUD, and Independent Agencies
Committee on Appropriations
United States Senate

The Honorable Jerry Lewis
Chairman

The Honorable Louis Stokes
Ranking Minority Member
Subcommittee on VA, HUD, and Independent Agencies
Committee on Appropriations
House of Representatives

Comments From the Department of Housing and Urban Development



U. S. Department of Housing and Urban Development
Washington, D.C. 20410-5000

August 4, 1998

OFFICE OF THE ASSISTANT SECRETARY
FOR PUBLIC AND INDIAN HOUSING

Ms. Judy England-Joseph
Director, Housing and Community
Development Issues
United States General Accounting Office
Washington, D.C. 20548

Dear Ms. England-Joseph:

Attached please find HUD's comments on your draft report entitled Section 8 Housing Assistance: HUD Plans to Recapture Over \$400 Million of Excess Funding in the Moderate Rehabilitation Program (GAO/RCED-98-235).

In general, HUD agrees with GAO's assessment of the steps now being taken to properly report to Congress the amount of excess budget authority in this program. The attached comments provide clarification of certain technical issues referenced in the draft report.

Thank you for the opportunity to review this document. We would be pleased to meet with you further to discuss the attached comments. To arrange such a meeting or to discuss other issues related to our concerns, please contact Nanci Gelb at (202) 708-0440.

Sincerely,

A handwritten signature in cursive script, appearing to read "Deborah Vincent".

Deborah Vincent
General Deputy Assistant
Secretary

Attachment

**Appendix I
Comments From the Department of Housing
and Urban Development**

Comments on GAO Report on Recapture of Excess Funding in the Mod Rehab Program

The following language insertions will help clarify programmatic information contained in the draft report:

Footnote deleted.
See footnote 3 on p. 1.

Page 1, footnote #1. The second sentence, with an additional third sentence, should read: "For most Section 8 project-based assistance, HUD contracts directly with the owners of private rental housing and state finance agencies to provide housing assistance for specific properties. Mod Rehab (including SRO) and project-based certificates, administered by state and local housing agencies, are the two exceptions."

Now on p. 3.

Page 4, first paragraph, line 8. The first full sentence should read: "For project-based assistance other than PIH-administered Mod Rehab or project-based certificates, HUD contracts directly with and provides rental subsidies to the owners of private rental housing and to state finance agencies."

See footnote 3 on p. 1.

Page 5, second paragraph. After the first sentence, insert sentence reading: "Mod Rehab SRO projects have 10 year HAP contract terms."

Now on p. 4.

Page 5, second paragraph. The fourth sentence should read: "In calendar year 1997, about 25 percent of these expiring HAP contracts were renewed as 1-year Mod Rehab contracts". An updated report with calendar year 1997 Mod Rehab activity was faxed to GAO on July 27, 1998. In summary, the report identified:

- 1-year renewals, \$31,466,771 for 4,681 units
- Replacement Certificates, \$73,123,697 for 13,364 units
- Replacement Vouchers, \$2,085,804 for 396 units
- Total: \$106,676,272 for 18,441 units.

Now on p. 5.

Page 7, first paragraph, last sentence should read: "HUD's Central Accounting and Program System is designed to capture the data necessary to calculate the total amount of excess budget authority that has accumulated in the program on an annual cycle as the HA reports actual program costs to HUD."

Now on p. 6.

Page 7, second paragraph, last sentence should read: "HUD did not recapture excess reserves from the Mod Rehab program in September, 1997 because Public Law 104-208, which provided the Secretary of HUD with authority to recapture Section 8 reserves, only applied to the certificate and voucher programs."

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