COMPTROLLER GENERAL OF THE UNITED STATES

B-114860

Dear Mr. Chairman:

The General Accounting Office has examined into certain operations carried out by the Department of Housing and Urban Development. Pursuant to your request dated July 24, 1970, we are reporting in three enclosures the results of our studies on (1) certain instances where it appears that the objectives and goals originally established for the rent supplement program are not being achieved (enclosure I), (2) the questionable financial stability of insurance funds administered by the Department (enclosure II), and (3) the significant variances in eligibility requirements for federally assisted housing programs (enclosure III).

Enactment of the proposed Housing and Urban Development Act of 1970 (S. 3639, 91st Cong., 2d sess.) would establish a subsidized multifamily housing program, patterned after section 236 of the National Housing Act, that would replace the present rent supplement program. The proposed legislation would also establish eight mortgage and loan insurance programs--replacing the various insurance programs authorized by the National Housing Act--which would be serviced by two of the four existing insurance funds administered by the Department.

In addition, the proposed legislation would standardize the basis for determining income eligibility for the federally subsidized housing programs to be established by the proposed legislation.

Although we have not obtained written comments of the Department on the contents of the enclosures, we have discussed the contents with appropriate Department officials and have considered their views in the final preparation of this report.

As agreed by the staff of your Subcommittee, we are making copies of this report available to the Secretary of Housing and Urban Development.

We plan to make no further distribution of this report unless copies are specifically requested, and then distribution will be made only after your agreement has been obtained or public announcement has been made by you concerning the contents of the report.

Sincerely yours,

Elmer B. Staats

Comptroller General
of the United States

Enclosures - 3

The Honorable John Sparkman, Chairman
Subcommittee on Housing and Urban Affairs
Committee on Banking and Currency
United States Senate

GENERAL ACCOUNTING OFFICE

COMMENTS ON SELECTED ASPECTS OF THE

RENT SUPPLEMENT PROGRAM

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

INTRODUCTION

The Housing and Urban Development Act of 1965 (12 U.S.C. 1701s) authorized a program of Federal rent supplements to enable private enterprise to provide housing for low-income people. The housing, whether acquired through rehabilitation of existing structures or through new construction, must be approved for mortgage insurance by the Department of Housing and Urban Development (HUD) under section 221(d)(3) of the National Housing Act (12 U.S.C. 1701 _et_ _seq_.) at market-interest rates, except for a limited number of projects authorized for mortgage insurance at below-market-interest rates.

During our review, we examined the administrative policies, procedures, records, and files of HUD and the project sponsors and had discussions with their representatives and with various project management officials. The review was performed at HUD headquarters in Washington, D.C.; at HUD regional offices in Chicago, Fort Worth, Philadelphia, and San Francisco; and at selected HUD insuring offices and locally sponsored rent supplement projects, and it included an examination of 20 market-interest-rate projects administered by the above HUD regional offices. At the time of our review (June 1969), 134 market-interest-rate projects were in operation nationwide.

Rent supplement payments for fiscal year 1969 totaled about $5.7 million, of which $650,000 applied to the 20 projects covered in our review. Not all the 20 projects had been in operation the full year. Total annual payments for the 20 projects will be about $1 million.

LIMITED ACHIEVEMENT OF ECONOMIC INTEGRATION

One of the major goals to be achieved under the rent supplement program has been the integration of low-income tenants receiving Federal rent supplements with ~~and~~ higher income tenants paying the full rent, referred to as economic integration. Our review of congressional hearings indicated that a substantial number of units in rent supplement projects would be occupied by tenants paying the full rent.

Our review revealed that economic integration was not being achieved in eight of the 20 projects and was being achieved only to a limited extent in the remaining 12 projects. A total of 886 units were available for occupancy in the 12 projects but only 45 (about 5 percent) were occupied by tenants paying full rent. In the eight projects, 649 of the 677 units were occupied by tenants receiving rent supplements; the remaining 28 units were not rented.

As a further indication of the degree of economic integration being achieved or planned, the latest available HUD statistics showed that, as of early fiscal year 1970, 99.6 percent of the dwelling units in the 185 market-interest-rate projects under rent supplement payment were occupied by tenants receiving rent supplements. For an additional 470 projects for which rent supplement funds had been reserved, 99.2 percent of the planned units were designated and approved by HUD for occupancy by tenants receiving rent supplements.

Such a designation, which is used as a control over rent supplement funds, is used to determine the maximum rent supplement payments HUD would be obligated to pay if all units so designated were actually rented to tenants receiving rent supplements. The designation, therefore, does not preclude project sponsors from renting units to tenants capable of paying the full rent.

On the basis of the tenant composition in the 20 projects included in our review, the designations for the 470 projects appeared to be generally representative of the actual tenant makeup of the projects for which rent supplement payments were being made.

In HUD's fiscal year 1969 appropriation hearings, HUD officials stated that economic integration in rent supplement projects should be accomplished over a period of several years through increases in the incomes of project tenants who may elect to remain in the project even though no longer eligible for rent supplement assistance.

Project sponsors and HUD officials told us, however, that a substantial number of the tenants of rent supplement projects were receiving welfare, social security, or other forms of assistance and had little potential for reaching higher income levels. HUD statistics showed that, as of December 1969, the primary source of income of approximately 58 percent of tenants receiving rent supplements was derived from such assistance payments; the primary source of income for approximately 42 percent of these tenants was salary and wages. The average annual income for all tenants receiving rent supplements was $2,350. We were told that, in selecting tenants for rent supplement units, consideration generally was not given to prospective tenants' potential for increasing their income.

Our test of income sources for 469 tenants receiving rent supplements in seven of the 20 rent supplement projects included in our review showed that 217 tenants were welfare recipients, 101 were receiving social security benefits or other assistance, 122 were employed, 21 were employed and also receiving assistance, and eight had other sources of income. The average total annual income, including assistance payments for 442 of the 469 tenants, was $4,000 or less. Of the 143 tenants who were employed, including those who were also receiving some form of assistance, 124 had annual incomes of $4,000 or less and over half had incomes of $3,000 or less.

A further test covering two projects where 60 recertifications of tenant income had been completed showed that, of 44 tenants receiving welfare assistance at initial occupancy, 43 were still receiving welfare assistance 1 year later. Of the remaining 16 tenants who were employed at initial occupancy, 15 were employed 1 year later--one became unemployed and went on welfare.

Since many tenants receiving rent supplements are receiving welfare or other forms of assistance and since, in selecting tenants, consideration is not given to prospective tenants' potential for increasing their incomes, it appears to us that it will be difficult for tenants receiving rent supplement payments to raise their incomes to a level where rent supplement payments will be substantially reduced or eliminated.

When we discussed the objective of economic integration with HUD regional officials and with project sponsors and managers, many of them expressed the opinion that economic integration would be difficult to achieve and that the limited number of tenants then paying the full market rent in rent supplement projects would reside there only until other suitable housing became available. Various reasons were given to us as to why economic integration would not be achieved to any significant extent--the most frequent reason was that people of higher income who could choose the neighborhoods in which they wished to reside preferred not to live in rent supplement projects.

Also, in several areas where rent supplement projects were located, our review showed that housing units were renting on the regular commercial market at rates comparable to or less than the full market rental rates approved by HUD for rent supplement projects. For example, in Atlantic City, New Jersey, a commercial apartment project was renting one-bedroom air conditioned units at monthly rates ranging from $120 to $125 while the rental rate for a one-bedroom rent supplement unit (not air conditioned) ranged from $127 to $131.

A management official of a rent supplement project in New Mexico stated that regular standard housing, comparable to rent supplement housing, generally rented at lower rates than those charged for rent supplement units. A project sponsor in California advised us that individuals could find regular standard housing in more desirable locations at rates comparable to the rental rates of rent supplement projects.

A HUD official told us that differences in prevailing rents for housing projects could be attributed to a variety of factors and could depend to a large extent on the level of construction costs and financing costs prevailing in the area at the time a project is developed.

Matters for consideration of the Committee

In view of the foregoing information, we believe that, if the objective of economic integration is to be achieved in the rent supplement program, the Committee may wish to explore what steps would be appropriate to promote such an objective.

Under the proposed housing act of 1970 (S. 3639, 91st Cong., 2d sess.), HUD would be prohibited from entering into new contracts for rent supplement payments. Instead, section 502 of the proposed legislation would establish a new subsidized housing program, patterned after the housing assistance program presently authorized by section 236 of the National Housing Act, under which the Secretary of HUD would be authorized, for the purpose of reducing rentals for lower income tenants, to make periodic assistance payments to mortgagees on behalf of the owners of multifamily housing projects. If the Committee believes that economic integration should be promoted in the proposed section 502 program, it may wish to explore what steps would be appropriate in light of the experience encountered under the rent supplement program.

LIMITED USE OF PROGRAM IN MAJOR URBAN CENTERS

When the rent supplement program was enacted into law in 1965, it was described by the Administration as "the most crucial new instrument in our effort to improve the American city."

At the time of our review (June 1969), there were no market-interest-rate rent supplement projects in operation in such major urban centers as Chicago, Detroit, and Philadelphia; and a total of three projects providing 230 units were in operation in the Los Angeles and San Francisco areas. HUD officials advised us that, as of September 1969, there were two projects with 525 units under payment in Detroit; four projects under contract in both Philadelphia and Los Angeles; and one project under contract in San Francisco. Greater use of the program was being made in two other major urban centers--Cleveland and Dallas--where approximately 1,800 rent supplement units were being constructed in poverty areas, in inner city blighted areas, and within the general vicinity of the urban centers. As of September 1969 there were 185 rent supplement projects under payment having a total of about 17,000 units.

Because of the limited amount of construction of rent supplement projects in highly urbanized areas, the program has not been effective in helping to meet low-rent housing needs. HUD regional officials stated that it was HUD policy to provide as wide a geographic distribution of these projects as possible and to locate projects in small towns and rural areas to the extent possible, particularly in those areas not served by public housing, so that the program would serve all the people who were in need, not just those residing in urban areas.

HUD regional officials and project sponsors explained that the limited extent of program participation in major urban areas was attributable to such things as (1) the scarcity of land in parcels large enough to attract adequately qualified sponsors, (2) high land and construction costs, coupled with maximum rental rates that make construction of projects in certain areas financially infeasible, (3) the lack of tax abatements or land value write-downs, (4) the reluctance of potential sponsors to become involved in the administrative procedures required to take advantage of Federal housing programs and to become involved in the sociological problems inherent in the management of this type of project, and (5) the high rate of crime.

HUD regional officials stated that, in the Cleveland area, local participation had been good primarily because of the interest and work of church organizations to better the living conditions of inner city residents and because neither the cost nor the availability of land had been major impediments. They stated also that, in the Dallas area, sponsor participation had been excellent because the cost of construction in the urban areas was no higher, and was sometimes less, than in areas less heavily populated.

According to several sponsors, more rent supplement projects could be constructed in urban centers if the projects could be located on urban renewal land. Title I of the Housing Act of 1949, as amended (42 U.S.C. 1450), provides that, upon approval of the Secretary of HUD, any real property held as part of an urban renewal project may be made available for new or rehabilitated housing for individuals of low or moderate income. In addition, HUD's regulations provide for selling such land at prices which would be attractive to sponsors of rent supplement projects.

A HUD quarterly report (first quarter of fiscal year 1970) on the rent supplement program showed that a small percentage (about 10 percent) of rent supplement projects in operation were located in urban renewal areas.

Matters for consideration of the Committee

We believe that, to encourage the development of rent supplement projects in major urban centers, consideration should be given to making greater use of urban renewal land. We believe also that maximum rental rates for rent supplement projects should be established on the basis of the income needed to make development of a project financially feasible in a particular area. The Committee may wish to have the Secretary of HUD take action along these lines to help make the rent supplement program more effective in improving the American city.

Under proposed housing legislation of 1970, the rent supplement program would be replaced by a subsidized rental housing program (section 502) patterned after the program presently authorized by section 236 of the National Housing Act. If enacted, section 502 should help to promote the construction of privately owned projects for low-income people in large urban centers because the HUD-approved maximum rents are to be representative of the fair market rental rates that would make the construction of such housing projects financially feasible in the particular area involved. The Committee may wish to have this proposed section also provide for greater use of urban renewal land for such housing projects.

LIMITED ACCOMMODATION OF LARGE LOW-INCOME FAMILIES

Construction of units with four or more bedrooms was limited or nonexistent in market-interest-rate rent supplement projects. For areas under the jurisdiction of HUD's Los Angeles, San Franciso, and Cleveland insuring offices, where HUD regional officials generally acknowledged a need for larger units, of a total of 3,684 rent supplement housing units occupied or under construction as of June 30, 1969, 92 contained four or more bedrooms. Also, no units of this size had been constructed under the program in the area of the Detroit insuring office, although HUD regional officials agreed that there was a definite need for such larger units.

HUD regional officials and project sponsors stated that the primary reason that housing units containing four or more bedrooms were not being planned or constructed was that (1) higher construction costs, (2) coupled with HUD's nationwide limit on the maximum rent that could be charged for such units, made the construction of larger units in rent supplement projects financially infeasible. ?

In May 1966, HUD issued instructions relating to maximum monthly rentals for living units in rent supplement projects. The instructions provided that the maximum monthly rentals for three or more bedroom units would be $140 with the provision that in high cost areas the maximum rentals could be increased by up to 25 percent. Under these rental rates, four-, five-, and six-bedroom units were subject to the same maximum monthly rate as three-bedroom units which were less costly to construct.

The maximum monthly rental rates have since been increased and, starting in early fiscal year 1969, a higher maximum rental rate was established for four-bedroom units than for three-bedroom units. However, four-, five-, and six-bedroom units still have the same maximum monthly rental rate ($177), which could be increased by 25 percent in high cost areas. It appears that the additional costs of constructing five- and six-bedroom units, without corresponding increases being allowed in applicable rental rates, would continue to discourage the construction of such units. According to HUD officials, the Department is currently reviewing these limits in light of construction cost increases since the present limits were established.

Other factors which HUD regional officials and sponsors said tended to discourage the construction of larger units were (1) the difficulty of designing a structure to include larger units, (2) the space required, (3) the fact that larger units generally result in higher maintenance costs, and (4) the reluctance to locate a number of large families in one building.

A HUD regional official stated that the program was serving the largest population segment by providing projects of three bedrooms or less. Some officials stated that the housing needs of large low-income families were being provided in leased single-family dwellings or in public housing projects designed for larger units.

Matters for consideration of the Committee

We believe that, if larger dwelling units are to be constructed under the program, the maximum rental rates established by HUD for larger size units should be commensurately greater than those for smaller size units. The Committee may wish to have the Secretary of HUD provide for more flexibility in the establishment of allowable maximum rents under the rent supplement program so that construction of dwelling units for larger families will be encouraged.

Under title I of the proposed housing act of 1970, the Secretary of HUD would establish the development cost for different sizes of homes and multifamily dwelling units in each housing market area. The development cost would be determined by establishing for each housing market area the "total construction cost" of a standard-sized new single-family home and a standard-sized dwelling unit in a new multi-family structure on the basis of plans and specifications for modest dwellings.

On the basis of these determinations, the Secretary would establish the total construction cost of various sizes of dwellings (more or fewer bedrooms). The total construction cost of the various sizes of dwellings would then be increased by the same percentage as that which the average cost of land and site improvements in the area bears to the total construction cost for similar sizes of homes and multifamily units in the area. Therefore, it appears that construction of larger units will be financially feasible since the total construction cost of such units will be representative of the costs in the area in which the projects are to be constructed.

Also, title V provides that, for each dwelling unit in an assisted project, a "basic rental" be established based on the costs of operating the project with the benefit of assistance payments attributable to the unit. The tenant would pay the basic rental for his unit or such greater amount not exceeding the fair market rental for such unit (the rental without subsidy).

The proposed bill also provides that up to 20 percent of the total amount of contract authority authorized by appropriation acts could be used for special projects in which all the units would be subsidized. These would be comparable to rent supplement projects under the present law. In such projects, payments equal to the difference between the sum of the monthly economic rent required for each unit in the project and the sum of the monthly basic rental established for each unit in the project would be made to the mortgagee. It appears, therefore, that some of the projects would enable sponsors to receive full economic rental and would enable low-income tenants to afford larger units.

We believe that, if enacted, the above proposed sections should help promote the construction of dwelling units for larger low-income families.

GENERAL ACCOUNTING OFFICE

COMMENTS ON THE FINANCIAL CONDITION OF INSURANCE FUNDS ADMINISTERED BY THE DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

INTRODUCTION

The four insurance funds maintained by the Department of Housing and Urban Development (HUD) have been authorized by the National Housing Act (12 U.S.C. 1701 et seq.) for the purpose of conducting the numerous mortgage and loan insurance programs under which lending institutions are insured against losses on first mortgages and loans made to qualified borrowers (mortgagors) for various types of housing and home improvements. These funds are (1) the Mutual Mortgage Insurance Fund, (2) the General Insurance Fund, (3) the Cooperative Management Housing Insurance Fund, and (4) the Special Risk Insurance Fund. From inception of the mortgage and loan insurance programs in 1934 to June 30, 1969, about $132 billion of insurance had been written, and about $63 billion of that amount was in force at June 30, 1969.

The insurance funds are charged with the administrative expenses of the insurance programs, the insurance claims of lenders arising from mortgage and loan defaults, and an allowance for estimated future losses on disposal of property and notes acquired and on hand. The funds are credited with income from insurance premiums, fees, investment income, and the proceeds from sales and rentals of acquired properties and sales of notes. The accumulated differences between the income of the funds and the expenses charged against the insurance funds are considered to be the insurance reserves available to cover future losses and administrative expenses. The combined total of net insurance reserves of the four insurance funds at June 30, 1969, was about $1.4 billion.

In determining the adequacy of its insurance reserves, HUD estimates, on the basis of actuarial studies of the risks underwritten, the probable future losses and related expenses for outstanding mortgages and loans that might be incurred if an economic reversal of depression magnitude were to develop immediately. HUD considers that an insurance fund is actuarially sound when the reserves are equal to, or greater than, the estimated reserve requirements for outstanding mortgages and loans.

FINANCIAL CONDITION OF INSURANCE FUNDS

The following table shows, for the four insurance funds combined, the estimated reserve requirements, the insurance reserves, and the estimated reserve deficiencies as of June 30 for the past 6 years.

Year	Estimated reserve requirements (note a)	Insurance reserves	Estimated reserve deficiencies
	(000,000 omitted)		
1964	$1,400	$1,120	$280
1965	1,520	1,130	390
1966	1,670	1,130	540
1967	1,700	1,180	520
1968	1,780	1,260	520
1969	1,910	1,400	510

[a]Excludes reserve requirements for below-market-interest-rate mortgages insured under section 221(d)(3). Premiums on these mortgages have been waived by HUD, and the General Insurance Fund is to be reimbursed from appropriated funds for any net losses.

The financial condition--estimated reserve requirements, insurance reserves, and estimated reserve surpluses or deficiencies--for each of the four funds as of June 30, 1969, was as follows:

Insurance fund	Estimated reserve requirements	Insurance reserves or negative reserves(–)	Estimated reserve surpluses or reserve deficiencies(–)
	(000,000 omitted)		
Special Risk	$ 20	$ –1	$ –21
Cooperative Management	21	23	2
General	497[a]	196	–301[a]
Mutual Mortgage	1,368	1,176	–192

[a]Excludes reserve requirements of $134 million for below-market-interest-rate mortgages insured under section 221(d)(3).

Special Risk Insurance Fund

Should be Guarantee Fund.

Established in 1968, this fund services mortgages insured pursuant to section 223(e), or insured under sections 235, 236, and 237 of the National Housing Act. These programs generally include the insurance of mortgages for families of low or moderate income, families who are poor credit risks, or families purchasing properties in older, declining urban areas. Because of the unusual risks insured, the Special Risk Insurance Fund was not intended to be actuarially sound and was authorized by law to receive appropriated funds to cover program losses. As of June 30, 1969, the fund had a loss (negative insurance reserve) of about $1 million; however, no appropriated funds have been received or requested by HUD to cover this loss.

Cooperative Management Housing Insurance Fund

Established in 1965 to administer management-type cooperative housing projects insured under section 213 of the National Housing Act, this fund had about $23 million in insurance reserves as of June 30, 1969, of which about $2 million was in excess of HUD's estimated reserve requirements. In 1970 HUD distributed in dividend payments about $1.6 million of the surplus reserves to some 380 cooperative projects.

General Insurance Fund

Established in 1965 to consolidate the operations of 14 separate insurance funds, this fund services 34 separate mortgage and loan insurance programs authorized by the National Housing Act. These programs include 12 home programs, 16 multifamily housing programs, 4 property improvement programs, a group practice facilities program, and a land development program.

Because of operating losses during the 6 years ended June 30, 1969, insurance reserves in the fund, or the 14 predecessor funds, decreased from $363 million to $196 million while estimated reserve requirements--exclusive of the requirements for the below-market-interest-rate mortgages insured under section 221(d)(3)--increased from $388 million to $497 million. This increased the reserve deficiency from $25 million to $301 million, or 7 percent of the reserve balance to 154 percent.

In connection with the housing legislative proposals for 1967, your Committee requested HUD to furnish the Committee with a report on the soundness of HUD insurance reserves. Your Committee had expressed concern over the rising insurance losses in recent years and the widening gap between available reserves and reserve requirements, which seemed to be related to the insurance of high-risk mortgages. In a May 1967 letter to the Committee, HUD stated that reduction of the gap between reserves and estimated reserve requirements would depend on the relationship between future income and future expenses and losses. HUD stated also, with respect to the adequacy of premiums for individual programs, that a detailed study of insurance costs by program was under way and that from this study judgments of the adequacy of individual program premiums might be possible. ?

K

could it anything else?

The study to which HUD referred in its May 1967 letter to the Committee showed that a progressive decline had occurred during fiscal years 1960-66 in the level of net income from insurance operations after payment of operating expenses and establishment of an allowance for estimated losses on acquired properties and notes on hand. The decline in net income was attributed by HUD to a combination of factors including (1) successive liberalizations of loan-to-value ratios for both home and project mortgages, (2) extension of mortgage insurance to new programs (nursing homes, housing for the elderly, housing in urban renewal areas, housing for displaced families, etc.), (3) recession conditions in 1960-61, and (4) adverse developments in individual local economic housing situations. The HUD study concluded that sufficient experience had been gained since 1960 to suggest a high probability that premium rates were too low in both home and multifamily-housing mortgage insurance programs to ensure the self-sufficiency of HUD's combined insuring operations over an extended future period.

The HUD study showed also that operating costs for most home and multifamily housing mortgage insurance programs were significantly higher than the income received from the premium charges of 1/2 percent. The study covered 10 of the 23 active mortgage insurance programs included in the General Insurance Fund in June 1967--these 10 programs were part of the 25 active programs in the fund at June 30, 1969. The study showed the following premium costs which were based on the limited experience then available for the various programs, and which suggested the need for close examination of operations under those specific programs.

Program--applicable section of National Housing Act		Approximate premium cost (note a)
Home:		
213	Cooperative sales	1.3%
221	Moderate income	1.3
222	Servicemen	1.0
Multifamily:		
207	Basic rental	1.0
213	Cooperative management and sales (note b)	0.7
220	Urban renewal	1.1
221	Moderate income (market rate)	8.9
231	Elderly	6.2
232	Nursing homes	1.7
810	Armed services (impacted areas)	8.8

[a]Under the National Housing Act, the maximum premium rate for the section 222 program cannot exceed 1 percent; however, the act does not provide for a maximum premium rate for the other nine programs.

[b]Includes management-type projects insured under the Cooperative Management Housing Insurance Fund.

Although the premium requirements for the section 207 multifamily mortgage insurance program (1 percent) and the section 203 home insurance program (a maximum of 3/4 percent) were based on a longer period of experience than the premium requirements for the other HUD programs, the study showed that it would be very difficult to conclude that most of the new, innovative, high-risk programs would not continue to have higher premium requirements than the section 207 and 203 programs. Premium requirements for the section 203 program are discussed under the Mutual Mortgage Insurance Fund. (See p. 8.)

The study suggested the following possible courses of action.

> "1. Raise all [HUD] annual premium rates to the levels actuarial calculations show to be required. This approach would make [HUD's] normal programs less competitive with conventional financing. It would be particularly damaging to [HUD's] high priority, social purpose programs, because it would increase the cost of the programs for those least able to afford them.
>
> "2. Adjust [HUD] premiums to the required rate for the "economic soundness" programs (203 and 207) and seek appropriations to cover losses on the high priority, social purpose programs. This latter approach has already been taken, by inference, with the 221(d)(3) BMIR program. This is the approach which has always been taken in the VA program. Perhaps the time has come to accept the fact that the pioneering missions which [HUD] is being asked to undertake today cannot be covered through a reasonable insurance premium."

The study also recognized that other courses of action might be possible, such as tightening program requirements.

In summarizing the results of the HUD study in hearings in July 1967 before your Subcommittee on Housing and Urban

Affairs on the proposed housing legislation for 1967, the then-Commissioner of the Federal Housing Administration stated that HUD did not believe that the premiums and fees charged in many of the high-risk programs were adequate to cover possible losses. The Commissioner stated, however, that it was HUD's position that the Congress had established high-risk programs to meet special social purposes and that HUD was administering these programs in that fashion, recognizing that losses would perhaps exceed revenue in many of the programs. We were informed by a HUD official that a copy of the HUD study was not furnished to your Subcommittee.

As a result of the Subcommittee hearings, your Committee reported out a bill (S. 2700, 90th Cong.), providing for the establishment of home mortgage insurance programs for low- and moderate-income families, which would be serviced by a separate insurance fund. The bill provided that, in view of the social purpose of the programs, the fund could receive appropriations to supplement the income received by the fund. Although the bill was not enacted, similar provisions were included in the Housing and Urban Development Act of 1968 (12 U.S.C. 1707-1715y) and the Special Risk Insurance Fund was established. (See p. 3.) This act did not provide for the transfer to the Special Risk Insurance Fund those high-risk social-purpose programs insured under the General Insurance Fund.

Public Law 90-301, enacted May 7, 1968, authorized the establishment of a Commission to study mortgage interest rates and to make recommendations toward ensuring the availability of an adequate supply of mortgage credit at a reasonable cost to the consumer. In an August 1969 report to the President and to the Congress, the Commission stated, with respect to the actuarial determinations made by HUD, that some reduction in the premiums might be possible by adopting a more realistic calculation of risks. The Commission report pointed out that HUD's estimates of the insurance reserve requirements were based on the losses that might occur in the event of a major economic depression. The Commission report stated that this basis seemed overly conservative in view of the changed economic environment prevailing now in comparison with that of the 1930's when some of the HUD insurance programs were established. HUD officials informed us that its actuarial calculations of reserve requirements did indicate what would be required to meet serious recession conditions but that these conditions were substantially less severe than the depression of the 1930's.

As of June 30, 1969, losses of $310 million incurred by 24 of the 34 programs served by the fund were covered by the $506 million in insurance reserves accumulated by the other 10 programs. HUD had not determined whether the future income from outstanding insured mortgage loans would be sufficient to meet future expenses and losses and to liquidate the existing losses.

Mutual Mortgage Insurance Fund

The Mutual Mortgage Insurance Fund, established to underwrite the home mortgage program authorized by section 203 of the National Housing Act, had a reserve balance of about $1,176 million as of June 30, 1969. The insurance reserves needed to maintain the fund on an actuarially sound basis were estimated by HUD at about $1,368 million. The deficiency of $192 million was attributable by HUD, in part, to the insurance of new mortgages with higher loan-to-value ratios (higher risk mortgages) and longer maturities.

Since the establishment of the section 203 program in 1934, the loan-to-value ratios and maximum amounts for insured mortgages have been significantly increased. In 1934, HUD could insure a 20-year mortgage on a single-family home at 80 percent of its appraised value. The maximum permissible mortgage was $16,000. Pursuant to the Housing and Urban Development Act of 1969 (12 U.S.C. 1720), HUD can generally insure a single-family home mortgage based on loan-to-value ratios of 97 percent of the first $15,000 of appraised value, 90 percent of the value in excess of $15,000 but not in excess of $25,000, and 80 percent of the value in excess of $25,000. The mortgage term is generally 30 years and the maximum permissible mortgage is $33,000. The following table shows the median loan-to-value ratios for new and existing single-family homes insured by HUD under section 203 for selected years.

Year	Median loan-to-value ratio: New homes	Existing homes
1950	88.0%	77.8%
1952	83.7	77.9
1954	85.3	78.5
1956	86.6	82.9
1958	91.5	90.2
1960	93.5	92.6
1962	94.4	94.4
1964	94.5	94.8
1966	95.0	95.2
1968	94.4	95.2
1969	93.7	95.1

The successive increases in the loan-to-value ratio facilitated homeownership by reducing the amount of the downpayment by the mortgagor; however, they increased HUD's insurance risk. HUD charges an insurance premium of 1/2 percent on all home mortgages insured under the Mutual Mortgage Insurance Fund, regardless of the loan-to-value ratio and related risk.

Several studies have indicated that as the loan-to-value ratio or the term of a mortgage increases, a greater percentage of mortgages are defaulted. For example, the HUD study in 1967 showed that, on the basis of the 1957-65 experience, the rate of default substantially increased as the loan-to-value ratio and mortgage term increased. This is shown in the following table.

Loan-to-value ratio	Defaults as a percent of insurance written — Term of mortgage: 20 years	25 years	30 years
86 to 89%	3%	5%	7%
90 to 92	5	7	9
93 to 95	9	11	13
96 to 97	15	19	23

Also, a 1969 study of default risk on HUD-insured home mortgages made by Mr. George M. von Furstenberg, assistant professor of economics at Cornell University, showed that, as the loan-to-value ratio increased from 90 to 97 percent, the default rate increased significantly. Mr. von Furstenberg concluded that any group of mortgagors receiving insurance on a disproportionately large number of low-downpayment (high loan-to-value ratio) loans would benefit from premiums paid by mortgagors who receive insurance on lower risk loans when one premium rate was used for all insured mortgages and the insurance program was actuarially sound.

HUD's 1967 study of premium costs showed that the premium of 1/2 percent was insufficient to achieve the actuarial soundness of the Mutual Mortgage Insurance Fund because of the greater number of mortgages being insured with high loan-to-value ratios. The HUD study concluded that the actuarial soundness of the fund could be maintained if, instead of one premium rate for all home mortgages, a variable premium basis was established which provided for premiums of (1) 1/4 percent for insured mortgages with loan-to-value ratios of less than 90 percent, (2) 1/2 percent for insured mortgages with loan-to-value ratios of 90 to 93 percent, and (3) 3/4 percent for insured mortgages with loan-to-value ratios of 94 percent or more.

We estimated that, if the above variable premium rates had been applied to the 324,000 home mortgages insured in 1969 under section 203(b) of the National Housing Act, 61,000 (19 percent) would have been assessed a premium of 1/4 percent, 79,000 (24 percent) a premium of 1/2 percent, and 184,000 (57 percent) a premium of 3/4 percent.

Matters for the consideration of the Committee

The General Insurance Fund reserve deficiency increased during the past 6 years from $25 million to $301 million (or 7 percent of the reserve balance to 154 percent) because of a decrease of $167 million in the insurance reserve balance and an increase of $109 million in estimated insurance reserve requirements. HUD's 1967 study of premium costs for 10 of the 34 programs (25 active and 9 inactive) presently included in the General Insurance Fund indicated costs at that date which were substantially higher than existing premium rates. No action has been taken by HUD to increase any of these premium rates.

In view of the fact that the HUD study included only 10 of the 25 active programs in the fund as of June 1969 and in view of the continued depletion of the fund's reserve balance, we believe that the Committee may wish to have HUD make a current appraisal of the premium rates needed for future insurance activity generated under all active programs in order that actuarial soundness in the General Insurance Fund may be achieved.

Because studies have shown that the risk of default on insured mortgages varies with the loan-to-value ratio and term of the mortgage loan for home mortgage loans, the Committee may wish to direct HUD to establish a variable system of premiums for home mortgage loans similar to that suggested by HUD's 1967 study of premium requirements for the section 203 home mortgage program.

In 1969, the Commission on Mortgage Interest Rates questioned whether HUD's reserve requirements were established on an overly conservative basis. In view of this, the Committee may wish also to have HUD review, in conjunction with its study of premium requirements, the reasonableness of the basis used to determine the reserve requirements of the General Insurance Fund and the Mutual Mortgage Insurance Fund and the individual mortgage and loan programs served by these funds.

Proposed housing legislation for 1970

Senate bill 3639 of the ninety-first Congress proposes to establish eight mortgage and loan insurance programs, replacing the various programs presently authorized by the National Housing Act, which would be serviced by either the General Insurance Fund or the Special Risk Insurance Fund, depending on whether the mortgage or loan is an insurable risk or a special risk. Mortgages involving Federal subsidies would be classified as special risks and would be insured under the Special Risk Insurance Fund.

The Secretary of HUD would have authority to establish premiums, at such rates as he determines necessary, for mortgages and loans to be insured under the proposed programs. HUD envisions that premiums for the proposed insurance programs to be serviced by the General Insurance Fund would be established on an actuarially sound basis; however, these programs would provide for insuring mortgages similar to those insured under the 10 programs which were the subject of HUD's 1967 study. HUD's study showed that these 10 programs had higher premium costs than the established premium rate of 1/2 percent.

The proposed legislation also would permit generally higher loan-to-value ratios for insured home mortgages than those currently permitted by the National Housing Act.

We believe that, if premiums for mortgages insured under the proposed legislation are to be established on an actuarially sound basis, steps along the lines of our suggestions discussed above, concerning (1) a current appraisal of premium rates, (2) consideration of a variable system of premiums, and (3) a review of the basis for determining reserve requirements, are essential to provide a proper basis for any appropriate changes.

HUD envisions that the premiums for those insurance programs which would be established by the proposed legislation and insured under the General Insurance Fund would be fixed on an actuarially sound basis. Because these proposed programs would be included in the General Insurance Fund, which at June 30, 1969, had an estimated reserve deficiency of $301 million, the Committee may wish to consider whether the premiums for mortgages insured under the proposed programs would provide sufficient income to eliminate the existing reserve deficiency in the General Insurance Fund.

Under the proposed legislation, the Mutual Mortgage Insurance Fund and the Cooperative Management Housing Insurance Fund would continue to serve mortgage loans previously insured pursuant to sections 203 and 213 of the National Housing Act; however, no new mortgage loans would be insured under these two funds. Mortgage loans similar to those previously insured under these two funds would be included in the insurable risk programs and insured under the General Insurance Fund. The proposed legislation would not provide for the distribution of dividends from the General Insurance Fund for these new mortgage loans as is provided for mortgage loans insured under the Mutual Mortgage Insurance Fund and the Cooperative Management Housing Insurance Fund.

Because mortgage loans similar to those previously insured under the Mutual Mortgage Insurance Fund and the Cooperative Management Housing Insurance Fund, would not be entitled to dividend distributions under the proposed legislation, the Committee may wish to consider the inclusion of a provision in the proposed legislation which would provide either for the payment of dividends on mortgage loans similar to those insured under the Mutual Mortgage Insurance Fund and the Cooperative Management Housing Insurance Fund or for the elimination of dividend payments relating to mortgages insured under these two funds at the present time. The Department favors inclusion of a provision in the proposed legislation which would provide for dividend distributions.

GENERAL ACCOUNTING OFFICE

COMMENTS ON SELECTED ELIGIBILITY REQUIREMENTS

FOR ADMITTANCE TO FEDERALLY SUBSIDIZED HOUSING

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

INTRODUCTION

Our survey covered eligibility requirements for admittance to the following major subsidized housing programs administered by the Department of Housing and Urban Development. The first two programs were authorized by the United States Housing Act of 1937, as amended; the third program, by the Housing and Urban Development Act of 1965; and the last three by the National Housing Act of 1934, as amended.

1937

1. Low-rent public housing.
2. Section 23 leased housing.

1965

3. Rent supplement housing.

1934

4. Section 221(d)(3) below-market-interest-rate (BMIR) rental housing assistance.
5. Section 235 homeownership assistance.
6. Section 236 rental housing assistance.

Eligibility requirements have been established for each program either by law, by HUD administrative regulation, or by local housing authorities.

DETERMINATION OF QUALIFYING INCOME

Criteria for determining the amount of qualifying income for federally subsidized housing programs serving low- and moderate-income persons vary significantly between locations and programs. As a result, certain inequities exist for program applicants living in the same general area as to eligibility and housing opportunities under the various programs.

Also, the administration of the programs is made more difficult.

Income limits for low-rent public housing and leased housing are established by local housing authorities on the basis of various factors considered by them to have an effect on the rent-paying ability of a family. Consequently, housing authorities could, and often do, have significantly different income limits for these programs. Income limits for leased housing are generally the same as for conventional public housing, but they can be higher under certain circumstances.

For the rent supplement program, income limits established by HUD are required by law to be no higher than those of the public housing program in the community but they can be lower. For the section 221(d)(3) BMIR program, HUD has generally tied income limits to the cost of walk-up apartment construction (not to exceed the median income in the area in which the housing project assisted under the program is to be built). Such limits are therefore not dependent on public housing limits. The incomes of applicants under the section 235 and section 236 programs cannot exceed the "regular limit" of 135 percent of the public housing limit in the area or the "exception limit" of 90 percent of the section 221(d)(3) BMIR limit which HUD can apply in certain cases.

Under existing procedures, low-income families in the same general area could be eligible for admittance to federally subsidized housing in one community and not in another, or they could be eligible for one program and not for another in the same community. In four communities within 15 miles of each other in the Washington, D.C., metropolitan area, the following income limits were in effect at the time of our review for a family of four under the six major subsidized housing programs.

	Qualifying annual income limits (family of four)					
Community	Low-rent public housing	Section 23 leased housing	Rent supplement housing	Section 235 home ownership	Section 236 rental housing	Section 221(d)(3) BMIR housing
A	$4,800	$5,400	$4,800	$6,480	$6,480	$8,850
B	5,100	5,100	5,100	6,885	6,885	8,850
C	4,700	4,700	4,700	6,345	6,345	8,850
D	4,800	4,800	4,800	6,480	6,480	8,850

The inequities generated by the different income limits are compounded by the fact that income is defined or arrived at differently from program to program and from community to community.

In determining whether a family's income is within the qualifying limits established for all federally subsidized housing, certain exemptions and deductions are required by law or administrative regulation to be made from the family's gross income. These include such items as (1) exemptions for minor children, (2) deductions for income of minor children, (3) deductions for income of adults other than the principal wage earner, and (4) deductions for amounts paid for the care of children to permit employment of family members.

The following table shows the major deductions and exemptions allowed at the time of our review under the low-rent public housing and leased housing programs by the previously mentioned four communities in the Washington, D.C., area.

	Major deductions or exemptions from gross annual family income			
Community	Maximum deduction for earned income of each adult other than the principal wage earner	Maximum deduction for income of each minor	Exemption for each minor	Other
A	$1,000	$1,000	$100	10 percent of earned income
B	-	-	-	Cost of care for dependent children
C	1,000	1,000	100	Cost of care for dependent children
D	---$ 600 per person------ ---$1,200 " family------		-	10 percent of gross income

Under the other federally subsidized housing programs covered during our survey (rent supplement, BMIR, section 235 and section 236), there is no provision either by law or by regulation for granting a deduction for the income of adults of same household other than the principal wage earner. In the case of minors' income, however, all such income is deducted from the total family income in computing qualifying income under these programs. Under the rent supplement program and the section 235 and section 236 programs, the law allows a $300 exemption per year for each minor in computing qualifying income. No exemption for minors is provided under the BMIR program.

We examined into the eligibility requirements for low-rent public housing for six major cities. At the time of our review, HUD records showed that, in five of the six cities local housing authorities, in computing qualifying income, allowed deductions for income of adults other than the principal wage earner. In the sixth city, such deductions were not allowed. In four of the six cities, deductions were allowed for income of minor children; in the other two, such deductions were not allowed. Moreover, the amounts of deductions for income of both adults and minor children and the conditions under which they were granted varied significantly among the cities. For example, in the four cities that allowed deductions for income of minor children, the amount ranged from $85 a month per minor and a maximum of $255 per family to all of such income if the minor was a student.

Only two of the six cities allowed an exemption for miors in computing qualifying income for the public housing or leased housing programs. In both cases, the exemption was $100 a year per minor.

Matters for consideration of the Committee

In view of the inequities that result because of the significant variances for establishing qualifying income under the various federally subsidized housing programs, we believe that a need exists for definitive criteria and procedures for establishing income limits and deductions to be used in determining the eligibility of applicants for such programs. We recognize that income limits should vary across the nation in accordance with economic conditions in each area, but we believe that the basis for and method of establishing qualifying income should be standardized. The Committee may wish to require that the method of determining a family's eligibility for housing assistance be standardized for all federally subsidized housing programs.

The proposed housing legislation for 1970 (S. 3639) would establish the median income in the area in which the subsidized housing is located as the basis for determining income limits for all federally subsidized housing programs. In addition, for purposes of determining the eligibility of program applicants, the proposed legislation would uniformly define income as including the income of all family members from all sources, except that nonrecurring income and the earnings of minors could be excluded, as determined by the Secretary of Housing and Urban Development. The Committee may wish to specify what percentage of the median income amount computed for an area would constitute the maximum income limits for federally subsidized housing programs in that area.

HUD officials have testified that local housing authorities would continue to establish income limits for the conventional public housing and leased housing programs, the only restriction being that such limits could not exceed median income in the area, as provided in the proposed legislation. In view of the above testimony by HUD officials, the Committee may wish to require that income limits for conventional public housing and leased housing be determined on the same uniform basis as that contemplated for all other subsidized housing programs to be authorized by the proposed legislation.

ASSET LIMITATIONS

At some locations and under certain programs, the amount of an applicant's assets is considered in determining his eligibility for admittance to federally subsidized housing. At other locations and under other programs, asset holdings are not considered at all.

According to HUD regulations, asset limitations are mandatory requirements only for the rent supplement program and the section 235 homeownership assistance program. The limitations for the rent supplement program are $5,000 for low-income elderly and $2,000 for low-income nonelderly applicants. For section 235 housing, these limits are increased by $500 for each dependent plus an amount equal to the applicant's share of the mortgage payment for 1 year. HUD has encouraged local housing authorities to consider applicants' asset holdings in determining their eligibility for federally assisted housing under the conventional low-rent public housing program and the leased housing program; however, asset limitations have not always been established. There is no legal or administrative requirement that asset holdings be considered in determining tenant eligibility under the rental housing programs authorized by section 221(d)(3) and section 236.

In the four Washington, D.C., area communities discussed in the preceding section (see p. 2), ~~the~~ local housing authorities had established asset limitations for admittance to public housing ranging from $750 to $12,900. Two of the authorities had different limitations for elderly and nonelderly applicants; the other two authorities each had a single limitation for all applicants.

Widely varying asset limitations had been established for public housing applicants in the six major cities discussed in the preceding section. (See p. 4.) Separate asset limitations for elderly and nonelderly applicants had been established in one of the six cities; the other five each had a single limitation.

In our report to the Congress on the Administration of the Leased-Housing Program (B-118718, February 4, 1970), we stated that nine of the 11 local housing authorities included in our review had established asset limitations for the leased housing program. (Asset limitations for leased housing were generally the same as those applicable to the conventional low-rent public housing program.) The limitations ranged from $3,000 to $15,000 for elderly applicants and from $3,000 to $9,000 for nonelderly applicants.

One of the two authorities that did not have asset limitations had accepted two elderly tenants who, according to the authority's records, had savings of about $33,500 and $24,000. In contrast, an authority located only a few miles away had an eligibility policy that disqualified any applicant having assets in excess of $3,000, except in unusual cases upon the special approval of the authority's board of commissioners.

Matters for consideration of the Committee

In view of the widely varying restrictions on asset holdings, the Committee may wish to consider whether asset limitations should be established for determining the eligibility of applicants for all federally assisted housing and whether such limitations should be uniform, nationwide, for all federally subsidized housing programs or whether they should be uniform within the various programs depending on the income levels to be served.

The proposed Housing and Urban Development Act of 1970 contains no provision for establishing limitations on asset holdings of persons in the determination of their eligibility for federally subsidized housing programs. The Committee may wish to consider whether such a provision should be included for the federally assisted housing programs being proposed.