Meeting Our Nation's Housing Challenges

REPORT OF THE BIPARTISAN MILLENNIAL HOUSING COMMISSION
APPOINTED BY THE CONGRESS OF THE UNITED STATES

2002

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Report of the Bipartisan Millennial Housing Commission
Appointed by the Congress of the United States

Submitted to the

Committee on Appropriations
and Subcommittee for VA, HUD
and Independent Agencies

Committee on Financial Services
and Subcommittee on Housing
and Community Opportunity

United States House of Representatives

Committee on Appropriations
and Subcommittee for VA, HUD
and Independent Agencies

Committee on Banking, Housing
and Urban Affairs and
Subcommittee on Housing
and Transportation

United States Senate

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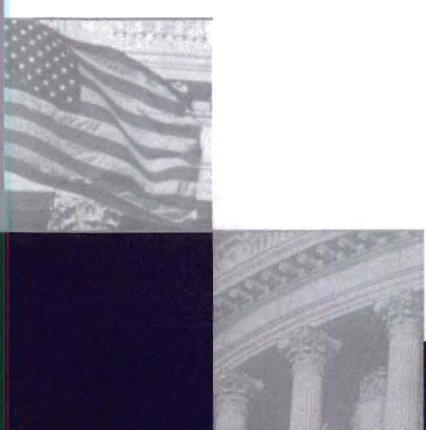




Executive Summary

Housing is most Americans' largest expense. Decent and affordable housing has a demonstrable impact on family stability and the life outcomes of children. Decent housing is an indispensable building block of healthy neighborhoods, and thus shapes the quality of community life. In addition, the housing sector provides a major stimulus to the nation's economy, consistently generating more than one-fifth of gross domestic product. Better housing can lead to better outcomes for individuals, communities, and American society as a whole.

In short, housing matters. This is why the federal government has long sought to expand the country's housing supply. Federal support for housing has taken many forms over the years: grants; subsidies on mortgage debt; direct payments to landlords on behalf of low-income citizens; the provision of liquidity and stability to the housing finance system through Federal Housing Administration mortgage insurance; the creation of the Federal Home Loan Banks, Fannie Mae, and Freddie Mac; and housing-related tax code measures, such as mortgage interest and property tax deductions, accelerated depreciation, tax-exempt mortgage financing, and Low Income Housing Tax Credits.

America's housing challenges cannot be described with statistics alone; they must be understood as a quality-of-life issues as well. Fundamental to the American Dream is somewhere to call home—a safe and welcoming "anchor place" where families are raised and memories are formed. Furthermore, housing must be viewed in the context of the community in which it is located. Improvements in housing need to be linked to improvements in schools, community safety, transportation, and job access.

Success in federal housing policy needs to be evaluated not just according to the number of housing units produced but also in terms of whether the housing produced improves both communities and individual lives. Federal housing assistance programs need to be reformed so that non-elderly, able-bodied people living in assisted housing have a personal responsibility, as do others, to contribute to society as well as accept its help. It is time for America to put these quality-of-life considerations on a par with cost considerations and make housing programs work to improve communities and individual lives.

In light of its mandate from Congress, the Millennial Housing Commission sought answers to some basic questions in seeking to address the nation's housing challenges:

- What is the importance of housing, particularly affordable housing, to the nation's infrastructure?
- Is the nation getting the housing outcomes it expects and desires for individuals, families, and communities? Are there better ways to meet these needs?
- How can the nation increase private-sector involvement?
- Are existing housing programs living up to their potential? Which need reform or significant restructuring?
- What are the critical unmet housing needs? Are new programs necessary to address these needs?

In the search for answers to these questions, the Commission held five public hearings, conducted numerous focus group meetings, commissioned papers, and solicited input on policy positions and program recommendations from a myriad of individuals and organizations. The consistent ideas expressed in these various forums were:

- Affordability and lack of decent housing are a growing problem, particularly for low-income families.
- Housing must be financially and physically sustainable for the long term.
- Housing issues are predominantly local issues, and programs must reflect the variations from state to state and community to community.
- Housing exists in a broader community context, and programs must consider the relation and impact of housing on education, economic opportunity, and transportation.
- Private-sector involvement in the production of affordable housing must be increased.
- Mixed-income housing is generally preferable to affordable housing that concentrates and isolates poor families.
- Consistent enforcement of the nation's fair housing laws is a vital part of making housing a part of the ladder of economic opportunity.
- Congruence among existing housing programs is essential.
- Homeownership counseling is necessary to make homeownership programs work well for low-income families.

These ideas are reflected in the Commission's recommendations to Congress.

New Tools

Enact a new homeownership tax credit.

The Commission recommends a state-administered homeownership tax credit, modeled on the successful Low Income Housing Tax Credit for rental housing. States would be able to use this flexible credit, under a qualified allocation plan, for two purposes. In qualified census tracts, where the cost to build or rehabilitate a unit will be greater than the appraised value of the completed home, states may use the credit to offset the developer's total development cost. A credit used in this manner would thus serve a community development purpose in addition to providing a new unit at a cost to the buyer that reflects local market conditions rather than the otherwise prohibitively high cost of development. Or, states may allocate the credit to lenders who in turn provide lower-cost mortgages to qualified buyers. In either form, the credit will extend the benefits of homeownership to low-income households and the communities in which they choose to live.

Support preservation with a broad system of tools, beginning with exit tax relief.

The stock of affordable housing units is shrinking. Some properties are in attractive markets, giving owners an economic incentive to opt out of federal programs in favor of market rents, and many owners have done so. Other properties are poorly located and cannot command rents adequate to finance needed repairs. In general, properties with lesser economic value are at risk of deterioration and, ultimately, abandonment, unless they can be transferred to new owners. To remove an impediment to transfer, the Commission recommends that Congress recognize and authorize "preservation entities," organizations that would acquire and own such properties and commit to the preservation of existing affordability. The Commission further recommends that Congress enact a preservation tax incentive to encourage sellers to transfer their properties to such entities. Subject to state housing finance agency oversight, an owner who sells to a preservation entity would be eligible for exit tax relief.

Provide capital subsidies for the production of units for occupancy by extremely low-income households.

This new tool would address the multiple problems of housing inadequacy that bear most heavily on extremely low-income (ELI) households, most of whom report paying well over half their incomes for housing costs. The most dramatic problem is the severe shortage of available units. No production program currently serves these households, and a significant portion of existing units that would be affordable to some of these families is occupied by higher-income households spending less than 30 percent of their incomes on housing. The capital subsidy would be used to produce new units and/or preserve existing units for ELI occupancy, eliminating debt on the units—and thus removing the debt service component from the household's monthly rental payment. No more than 20 percent of the units in any one development would have ELI occupancy restrictions. This program would thus result in more and better-quality units for ELI households and a degree of deconcentration of poverty.

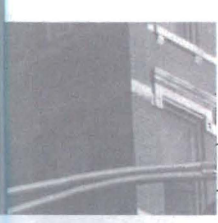
borrowed in private markets. If feasible, obsolete properties could be repositioned using the HOPE VI program. The recommendation also addresses troubled agencies, the program's overly complicated rent structure, and the disproportionate regulatory burden on small PHAs.

Revitalize and restructure the Federal Housing Administration within HUD.

Revitalizing and restructuring FHA is an urgent priority for congressional action. FHA's multifamily insurance is an indispensable tool for stimulating housing production, and its single-family insurance extends homeownership opportunities to low-income families and minorities. FHA's potential, however, is limited by its outmoded structure and confining statutes. The Commission therefore recommends that Congress restructure FHA as a wholly owned government corporation within HUD, governed by a board chaired by the HUD Secretary. Such a structure would enable FHA to adapt its programs to evolving markets without relying on Congress to legislate each change, and it could be accomplished with no substantial budget impact. It would also enable FHA to invest in technology, leading to increased efficiency and reduced risk, and to attract and compensate staff at competitive levels, securing the skills needed to manage its nearly $500 billion mortgage insurance program. Equally important is that under such a restructuring the FHA would remain with HUD and would be an effective force for the production and preservation of affordable housing. The Commission also outlines recommendations intended to provide FHA with more flexible multifamily and single-family operations. If Congress chooses not to restructure FHA, the MHC recommends that its proposed improvements be implemented within the current FHA organization.

End chronic homelessness.

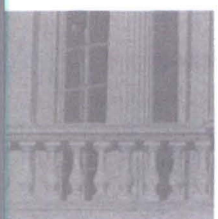
Homeless families and individuals generally fall into two categories: the transitionally homeless and the chronically homeless. Transitionally homeless households need adequate housing, first and foremost, while those who are chronically homeless confront health or substance abuse problems in addition to extreme poverty. With its capital subsidy for units targeted exclusively to extremely low-income households and its recommended improvements to public housing, vouchers, and the HOME and Low Income Housing Tax Credit programs, the Commission believes that the tools needed to end transitional homelessness will be available. For the chronically homeless, permanent supportive housing, which combines housing with intensive rehabilitative and other social services, is needed. The Commission recommends the elimination of chronic homelessness over a 10-year period by the creation of additional units of permanent supportive housing and the transfer of renewal funding for such units to HUD's Housing Certificate Fund.



would be occupied by working poor, including former welfare, households. For the HOME program, the Commission recommends substantially increased appropriations.

Improve the Mortgage Revenue Bond program.

State housing finance agencies (HFAs) issue Mortgage Revenue Bonds (MRBs) and use the proceeds to generate single-family mortgages. A statutory provision known as the "10-year rule" limits HFA use of scheduled repayments and mortgage prepayments and has resulted in substantial lost mortgage volume to date. This provision should be repealed immediately. In addition, as long as income limits are enforced, the Commission recommends repeal of purchase price limits, as well as restrictions that limit eligibility to first-time homebuyers and restrictions that apply in some states and limit eligible Veterans. These measures combined will help to ensure that HFAs maximize the public benefit associated with bond issuance in the interest of promoting homeownership for low-income families.



Revise federal budget laws that deter affordable housing production and preservation.

Budget laws inhibit the U.S. Department of Housing and Urban Development (HUD) from entering into contracts requiring more than one year's funding. As a consequence, HUD cannot offer the owners of multifamily housing multiyear contracts for rental assistance, and owners cannot obtain financing on the terms most advantageous for capital investment in the affordable housing stock. As a practical matter, Congress has never failed to appropriate funding to renew existing contracts for rental assistance. The Commission recommends, therefore, that funding for rental assistance be moved to the "mandatory" category of federal expenditures, so that private-sector lenders will be willing to finance repairs. The MHC suggests alternate measures that would have the same effect.

In addition to the principal recommendations described above, the Millennial Housing Commission endorsed a number of supporting recommendations: increase funding for housing assistance in rural areas; increase funding for Native American housing; establish Individual Homeownership Development Accounts to help more low-income households buy homes; allow housing finance agencies to earn arbitrage; exempt housing bond purchasers from the Alternative Minimum Tax; undertake a study of Davis-Bacon Act requirements; address regulatory barriers that add to the cost of housing production; streamline state planning requirements for community development programs; expand the financing options for small multifamily properties; foster a secondary market for development and construction lending; launch a demonstration project for comprehensive community development; improve consumer education about home mortgage lending; improve the access of manufactured home buyers to capital markets; affirm the importance of the Community Reinvestment Act; and affirm the importance of the government-sponsored enterprises.

One analysis conducted in Minnesota, comparing the unemployment rates and average earnings of welfare-to-work recipients with and without rental assistance, found that the combination of housing and job assistance resulted in much more favorable employment outcomes.[4] The evidence is therefore mounting that stable, affordable rental housing plays an important role in helping families find and hold jobs.

Other research suggests the stability that homeownership brings can have especially positive effects on school success and social behavior.[5] All else equal, children of parents who own their homes and live in neighborhoods with low turnover have a higher probability of completing high school.[6] Teenaged daughters of homeowners are also less likely to become pregnant.[7] Even after controlling for parents' age, income, and other influences, homeowners' children have significantly higher math and reading scores as well as significantly fewer behavioral problems and a better quality home environment than renters' children.[8]

The physical condition of housing makes a difference for families as well. Better-quality housing is related to lower levels of psychological distress, which in turn reduce health care costs and improve productivity.[9] In contrast, housing that exposes families to hazards such as lead paint can limit lifelong educational and economic achievement.[10] The presence of dust, molds, and roach allergens in the home increases the incidence of asthma and allergies, while electrical problems, poor lighting, and other system deficiencies increase the risk of illness, injuries, and even death.[11]

Neighborhood Quality and Access to Opportunity

The vast majority of Americans live in communities with good-quality schools and ready access to jobs. But for millions of households, particularly those living in high-poverty urban or rural areas, such opportunities are severely limited. Unemployment, crime, high-school dropout, and teen-pregnancy rates are all significantly higher in these locations.[12] The incidence of post-traumatic stress disorder, depression, and anxiety among inner-city youth is also higher.[13] These problems make it especially difficult for local residents to find decent paying jobs and to improve their lives by saving enough to invest in homeownership, higher education, and other wealth-enhancing measures.

As a result, neighborhood quality plays an important role in positive outcomes for families. Stable housing in an unstable neighborhood does not necessarily allow for positive employment and child education outcomes. Federal demonstration programs enabling the poor to move from distressed city neighborhoods to lower-poverty communities underscore the potent impact of neighborhood quality on family stability. Research from the Gautreaux and Moving to Opportunity demonstrations indicates that relocating families to better neighborhoods can improve educational, mental health, and behavioral outcomes.[14] Evidence of the impact of these programs on employment, however, is mixed.[15]

Neighborhood Revitalization

While relocating lower-income families is one way to support economic independence and individual advancement, so too is the revitalization of distressed neighborhoods. Without strengthening schools, providing access to services, and connecting residents to jobs, housing development by itself cannot provide a platform for opportunity.

Both theory and empirical evidence suggest that when several owners fail to maintain their properties, others nearby follow suit because their neighbors' inaction undermines property values. Rundown and abandoned properties can have a contagious effect that accelerates neighborhood decline.[16,17]

Replacing or upgrading distressed properties is therefore a precondition for neighborhood revitalization. Indeed, public investment in housing often triggers private investment that ultimately lifts property values.[18] Although larger economic and social forces can undermine such efforts,[19] recent comprehensive community development projects suggest that concentrated public investment in mixed-income housing can initiate neighborhood reclamation.

swings. As a result, U.S. citizens are some of the best-housed people in the world.

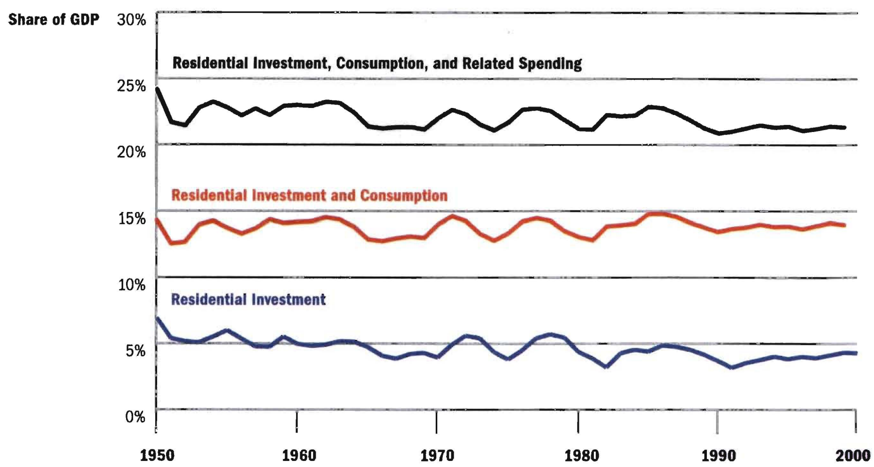
Not only does the nation's housing finance system provide unparalleled access to mortgage credit, but by doing so it also strengthens the overall economy. Without continuous access to mortgage credit on favorable terms, the nation's nearly $12 trillion investment in household real estate would be vulnerable to depreciation[28]—with cascading effects on home equity, consumer confidence, and the overall financial system (Fig. 3). Uninterrupted access to development and construction finance also helps to prevent disruptive swings in building activity.

For consumers, today's narrower spreads between interest rates on mortgages and Treasury securities have provided great savings. The introduction of automated underwriting has also led to lower origination and servicing costs. These benefits largely derive from the evolution of strong secondary markets. The federal government has developed a variety of mechanisms to ensure that Americans have continuous access to affordable credit, including the creation of Fannie Mae and Freddie Mac, mission-driven secondary-market companies dedicated to providing liquidity to mortgage markets and contributing to meeting affordable housing needs.

The Federal Housing Administration (FHA) is also a central player, reaching many underserved households that private lenders can not or do not reach. Together with Ginnie Mae, its secondary-market agency for packaging and selling loans, FHA has been the innovator of many mortgage products, insurance products, and mortgage-backed security designs that are now the mainstays of the housing market. Finally, the Federal Home Loan Banks (FHLBanks), also mission-driven, support residential lending through their members/shareholders.

Figure 2

Housing Consistently Contributes More Than a Fifth of GDP

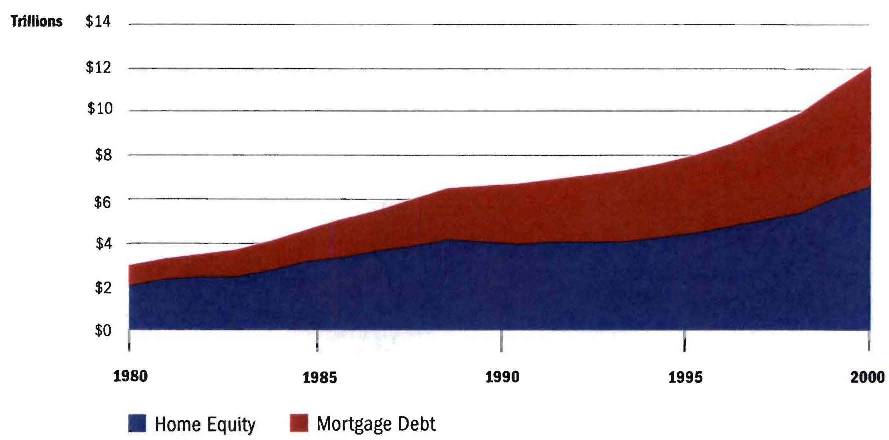


Note: Calculation includes use of gross residential investment, housing expenditures, and household operation expenditures, 1950-2000.

Source: Bureau of Economic Analysis, Personal Consumption Expenditures by Type, Gross and Net Investment by Type, October 2001.

Figure 3

Both Home Equity and Household Mortgage Debt Stand at Record Levels



Source: Federal Reserve, Federal Flow of Funds Data, Historical Data.

The stabilizing force of the housing finance system was apparent in the most recent economic cycle. When the economy softened in 2001, mortgage refinances and home sales helped to offset broader economic weakness, and residential investment remained steady. Following the events of September 11, 2001, Fannie Mae and Freddie Mac kept capital flowing even when stock and bond markets shut down.

To reiterate, housing does matter—in every aspect of society. For this reason, the Millennial Housing Commission is convinced that investment in housing production, preservation, and assistance will prove to be a cost-effective and life-enhancing investment in the future—and particularly for those millions of households who are otherwise unable to obtain decent, affordable, and stable housing.

The other most significant housing challenge facing the nation is the gap in homeownership rates between whites and minorities, as well as between high- and low-income households. Not all households that want to buy homes and are capable of managing the responsibilities of homeownership have been able to do so. Homeownership has the potential to help families build their assets and wealth, stabilize their housing costs and living arrangements, and gain greater control over their home environments. A balanced housing policy must therefore make addressing both the homeownership gaps and the rental affordability challenges urgent national priorities.

Scope of the Affordability Challenge

Most federal programs measure affordability by the relationship of income to housing costs. Spending 30 percent to 50 percent of income on housing is the generally accepted definition of a moderate affordability problem; spending more than 50 percent is considered a severe affordability problem. In reality, however, spending more than 30 percent of income for many lower-income households is a significant hardship that prevents them from meeting other basic needs or saving and investing for the future.

Under these definitions, 13.4 million renter households and 14.5 million owner households have housing affordability problems (Fig. 4). For cost-burdened renters, the struggle is to pay rent and utilities; for cost-burdened owners, the problem is keeping up with property maintenance as well as holding on to home equity.[3] Elderly and disabled owners, in particular, may be unable to perform the upkeep necessary to keep their homes in good repair.

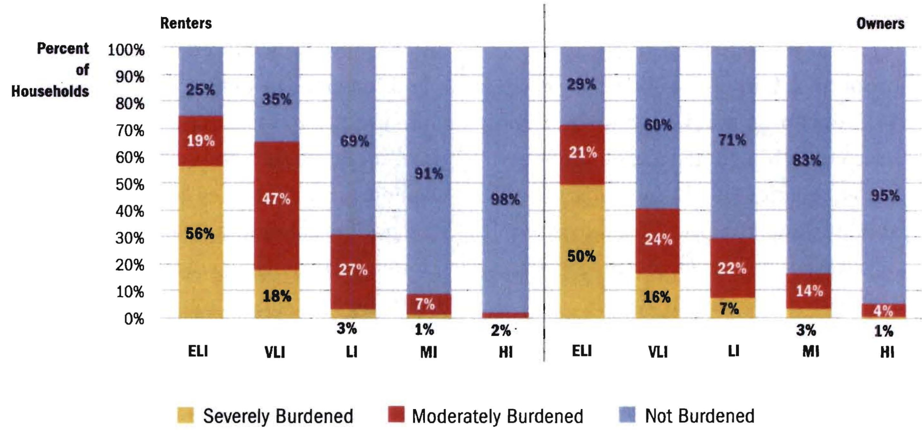
Households cannot afford housing for several reasons. In some cases, their incomes are too low to cover even modest rental housing costs. In others, they live in high-cost markets where having even a moderate income is insufficient to afford housing. In yet others, working families are unable to earn enough wages to manage their housing costs and basic needs because of age, disability, or difficulty finding full-time jobs.

In rare instances, families may choose to spend more than 30 percent of their incomes on housing simply because they consider it a top priority. But the fact that the average American household in 1999 devoted only about 20 percent of income for housing suggests that spending more than 30 percent is bred of necessity, not choice.

Federal housing policymakers have responded to these affordability challenges in a variety of ways: by producing additional units, by preserving existing low-cost units, and by assisting families in paying their rents or mortgages. While the Commission endorses such a balanced program, it has also concluded that more can and should be done to couple housing programs with measures to increase employment opportunities for working families and expand affordable housing options in areas of rapid job growth.

Figure 4

Many Owners as well as Renters Face Severe Affordability Problems



Source: HUD tabulations of the 1999 American Housing Survey prepared for the Millennial Housing Commission.

Definitions of Income Groups Used Throughout This Report

Extremely Low Income	(ELI)	=	At or below 30 percent of area median income (AMI)
Very Low Income	(VLI)	=	30.1 to 50 percent of AMI
Low Income	(LI)	=	50.1 to 80 percent of AMI
Lower Income		=	At or below 80 percent of AMI
Moderate Income	(MI)	=	80.1 to 120 percent of AMI
High Income	(HI)	=	Above 120 percent of AMI

Moreover, many families with earnings significantly higher than the full-time, minimum wage equivalent also face moderate and severe housing affordability problems. Consider household heads working in retail sales (with a median income of $15,940), licensed nursing ($27,850), or law enforcement ($37,560).[9] Among the 11.8 million households with earnings between the median for retail sales workers and the median for licensed nurses, fully 34 percent had moderate housing cost burdens, and 10 percent had severe problems. Among the 11.4 million with earnings between the medians for licensed nurses and law enforcement, 19 percent had moderate problems, and 5 percent had severe problems.

The Shrinking Rental Supply

Comparisons of renter households by income and the stock of units they can afford (at 30 percent of income) show a critical shortage of affordable apartments for extremely low-income households (Fig. 6). National figures, however, mask wide variations in affordability both within and across metropolitan areas. In addition, a substantial portion of the rental housing that is affordable to lower-income households is old and located in neighborhoods with little access to jobs or adequate facilities and services. Making matters worse, higher-income households outbid lower-income households for rental units in an effort to limit their housing expenses, sharply reducing the number of affordable units for others.[10]

Figure 5

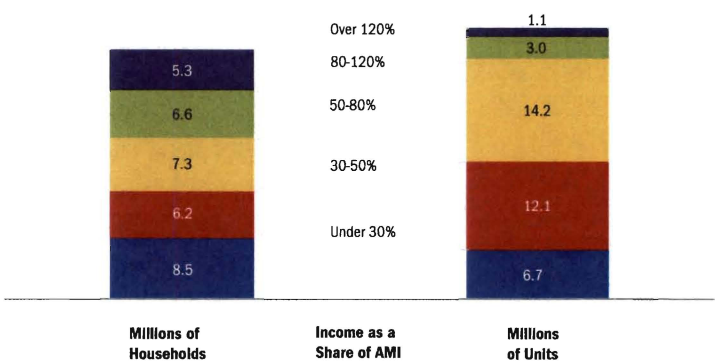
Housing Costs Far Exceed Lower-Income Households' Ability to Pay

Households	Number (Millions)	Share (%)	Median Reported Income	Monthly Housing Costs Affordable	Monthly Housing Costs Actual	Cost as % of Income
Renters						
Extremely Low Income	8.5	25	$7,000	$175	$426	58
Very Low Income	6.2	18	$17,000	$425	$509	35
Low Income	7.3	21	$26,541	$664	$565	25
Moderate Income	6.6	19	$40,000	$1,000	$643	19
High Income	5.3	16	$68,000	$1,700	$736	12
All	34.0	100	$24,400	$610	$560	25
Owners						
Extremely Low Income	6.4	9	$6,500	$163	$300	50
Very Low Income	7.1	10	$15,613	$390	$324	25
Low Income	10.7	16	$27,000	$675	$453	21
Moderate Income	14.3	21	$41,200	$1,030	$633	17
High Income	30.3	44	$81,000	$2,025	$908	13
All	68.8	100	$45,400	$1,135	$617	17
All						
Extremely Low Income	14.9	15	$7,000	$175	$369	54
Very Low Income	13.3	13	$16,000	$400	$426	31
Low Income	18.0	18	$27,000	$675	$520	23
Moderate Income	20.9	20	$40,050	$1,001	$637	18
High Income	35.6	35	$79,000	$1,975	$865	13
All	102.7	100	$36,000	$900	$585	19

Source: HUD tabulations of the 1999 American Housing Survey prepared for the Millennial Housing Commission.

Figure 6

The Affordability Squeeze from the Supply-Demand Gap Primarily Affects Extremely Low-Income Households



Source: HUD tabulations of the 1999 American Housing Survey prepared for the Millennial Housing Commission.

of-income standard) to households with incomes at the upper limit of each income category at each point in time.

Use of this method reveals that the number of units affordable to households in the extremely low- and very low-income ranges increased as a result of rising incomes. But the number of units affordable to those with incomes between 60 percent and 120 percent of area medians fell sharply (Fig. 7).

It would be incorrect to conclude from this analysis that there is no need to add directly to the stock of rentals affordable to ELI households. After adjusting for income growth, the supply of units affordable to such households is actually growing, but the existing gap between the number of ELI renter households and units in their affordable range reinforces the need for production. Even more important, a closer look at the rentals that are affordable and available to ELI households reveals that the supply remained dead flat despite the growth in number of units affordable to them. Apparently, the drop in the number of affordable rentals in the middle-income ranges led to increasing numbers of other renters occupying units affordable to ELI households.

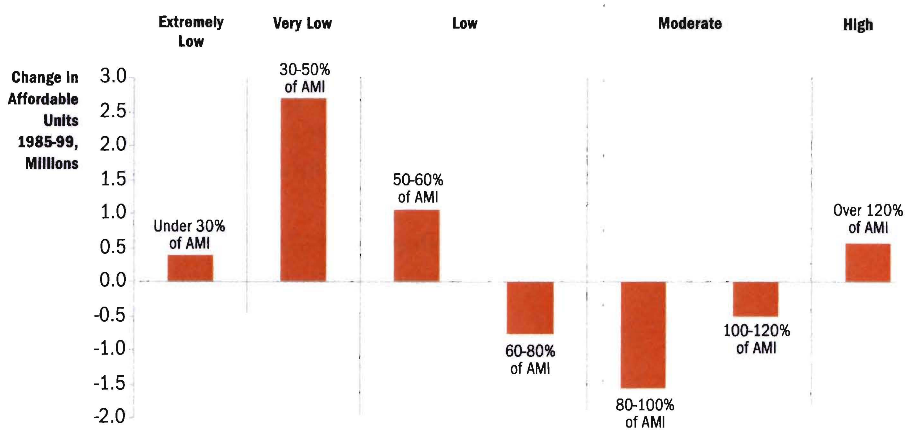
This result underscores the importance of producing many more units for working families with incomes between 60 percent and 120 percent of area medians. These units are disappearing at an alarming pace. As a result, a potentially important source of rentals that might later become available to lower affordable ranges is being lost.

In addition, rental housing production has tilted toward units affordable only to the upper reaches of the income distribution. In 2000, only 13 percent of all completed two-bedroom apartments were affordable to renters earning the median income in that year. Only about one-third of completed two-bedroom apartments rented for less than $750.[12] This largely reflects the fact that the private sector cannot produce apartments in most areas that are affordable to households with incomes under 70 percent of area median (and sometimes even higher) without a subsidy.[13]

It is clear that the nation's housing affordability problems have not retreated, even under the unusually favorable conditions of the 1990s and current levels of government aid. The federal government must therefore expand the resources and tools available to stimulate production of units both for extremely low-income households, where the greatest needs exist, and at the low- and moderate-income levels, where losses of affordable units are increasing the pressures on working families.

Figure 7

Affordability Pressures Are Mounting as the Moderate-Income Rental Supply Plummets



Note: HUD income limits are adjusted for inflation and real income growth for both 1985 and 1999.
Source: Appendix 1, Table 2.

Constraints on Production and Preservation

Several factors deter developers from producing affordable housing, particularly affordable multifamily housing. These obstacles include a lack of appropriate financing and the imposition of development controls. High development costs, reflecting stricter standards of construction and constraints on land supply, also play a role.

Persistent Homeownership Gaps

While most Americans aspire to homeownership, many face formidable barriers to achieving their goal. These obstacles include the high cost of housing generally, the costs specifically associated with buying a home, the underwriting standards applied by mortgage lenders, and the cost and availability of mortgage credit.

Owning a home provides many unique benefits and is an important step up the ladder of economic opportunity. Ownership creates greater security of tenure, greater control over one's own home environment, and opportunities to build equity while locking in current costs with fixed-rate loans.

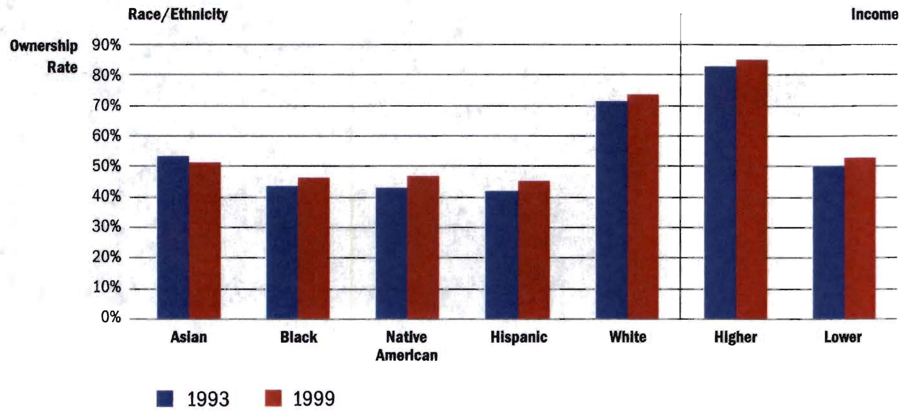
Homeownership also helps stabilize communities by increasing the number of resident owners who care about the quality of neighborhood life. Helping those willing and able to own homes to overcome the obstacles thus remains a significant national priority.

After a period of stagnation in the 1980s, evident progress was made in reaching out to low-income and minority homebuyers in the 1990s. Between 1994 and 2000, the number of lower-income homeowners increased by about 2.5 million, African-American owners by about 1.2 million, and Hispanic owners by about 1.2 million.[21]

Because the largest single constraint on lower-income borrowers is lack of savings,[22] the dramatic reductions in downpayment requirements opened the doors to homebuying for many. In 1990, only 3 percent of all loans were made with downpayments of 5 percent or less. By 2000, that share had risen to 16 percent.[23]

Figure 8

Despite Recent Gains, Minority and Low-Income Homeownership Rates Still Lag



Source: U.S. Bureau of the Census, Current Population Survey, 1993 and 1999.

Introduction of new risk management tools enabled lenders to relax underwriting standards and extend credit to low-downpayment borrowers. These tools also revealed that credit could be extended at higher housing-debt-to-income ratios than originally thought, provided borrowers have strong credit histories as measured by commercially available credit scores. Furthermore, the expanded use of automated underwriting systems lowered housing finance charges and removed individual discretion (and bias) from loan approvals. Finally, heightened regulatory pressures on Fannie Mae, Freddie Mac, banks, and thrifts to boost their purchases of loans to lower-income borrowers led to expanded marketing and outreach.

Even with all of these innovations, though, the homeownership rates of low-income families and minorities still lag those of higher-income families and non-Hispanic whites by large margins. As of 1999, the gap between black and white homeownership rates stood at 27.2 percentage points, the gap between Hispanic and white homeownership rates at 28.6, and the gap between lower-income (defined as 80 percent or less of AMI) and high-income (defined as greater than 120 percent of AMI) rates at 32.3 percentage points (Fig. 8).[24] A slim majority of lower-income households owns homes.

Differences in the average incomes and ages between minorities and whites explain some, but not all, of these gaps. Even if minorities owned at the same rate that whites of comparable ages and incomes do, the minority homeownership rate overall would still fall more than about 12 percentage points below that of whites.[25]

Lagging minority homeownership rates are a serious concern. Minority households are expected to account for two-thirds of household growth over the coming decade. Improving the ability of such households to make the transition to homeownership will be an especially important test of the nation's capacity to create economic opportunity for minorities and immigrants and to build strong, stable communities.

environment for every American family." The act also created the Urban Renewal (then called Urban Redevelopment) program, intended to improve communities by giving grants to localities to eliminate slums and blight by substantially reducing land acquisition costs. In addition, the act authorized funding for another 810,000 units of public housing, and took a first step toward addressing the housing needs of rural Americans by authorizing the U.S. Department of Agriculture to make loans and extend related assistance to low-income farmers.

During the 1950s, communities used Urban Renewal to fund demolition and redevelopment. The Housing Act of 1954 instituted a "workable program" requirement under which localities had to submit a plan for redevelopment—the first example of comprehensive planning being required for federal funding, a standard that continues to this day. The 1950s also saw development of a special program for nonprofit owners to provide housing for elderly or handicapped tenants, as well as continued growth in federal involvement in housing finance as the FHA became more active in insuring multifamily mortgages.

During the 1960s, the FHA introduced a wave of new housing finance programs to subsidize production of multifamily housing for low- and moderate-income families. Below-market interest rate loans and direct subsidies of various sorts, along with new tax write-offs, were added to spur private sector participation. While limiting owners' returns over the life of the program, the programs allowed owners to convert the properties to market rate rentals after 20 years. This program structure turned out to have perverse effects: at the end of the 20 years, the government lost the best-run and most attractive properties in good locations, and was left with the poorly located and managed properties that did not command high enough rents to cover the costs of capital preservation.

In 1965, the U.S. Department of Housing and Urban Development (HUD) was created as a cabinet-level department charged with overseeing the nation's housing and community development programs. The 1960s also marked the launch of a new approach—the ability of public housing authorities to rent privately owned units for their tenants. This precursor to housing certificates and vouchers enabled low-income families to rent privately owned units.

By 1969, some of public housing's poorest tenants were paying as much as three-fourths of their incomes for rent, and payments equal to one-half of gross income were common.[1] A series of amendments then eliminated PHAs' ability to set minimum rent levels and instead capped rents at 25 percent of tenant income. Congress addressed the resulting loss in PHA operating income in 1970 by introducing subsidies intended to cover the shortfall between rental income and operating expenses. Later, in the Omnibus Budget Reconciliation Act of 1981, Congress raised the minimum rents on public housing from 25 percent to 30 percent of income in an attempt to boost PHA income. In addition, HUD issued regulations pursuant to previously enacted legislation giving preference to families with severe housing problems.

The Housing and Community Development Act of 1974 brought about two major changes in housing programs. First, it consolidated seven categorical grant programs to localities into the Community Development Block Grant (CDBG) program, which continues to fund a broad array of community development initiatives. This program provided for local flexibility in how best to engage in community development, but required submission to HUD of a formal planning tool called the "Housing Assistance Plan." Second, the 1974 act amended the U.S. Housing Act of 1937 to create the Section 8 program, under which the subsidy covered the difference between a fixed portion of tenant income and the "fair market rent" for the unit, as defined by HUD. The program was primarily used by, but not limited to, the private sector. Section 8 was designed to give localities the flexibility to use the funds for new construction, substantial rehabilitation, or tenant-based assistance for occupancy of existing rental units. Long-term (20- to 40-year) subsidy contracts for Section 8 new construction and moderate rehabilitation facilitated the private financing of such developments.

In the early 1980s, additional tax incentives made development of affordable rental housing even more profitable. The Tax Reform Act of 1986 then repealed accelerated depreciation and use of depreciation deductions to offset other ordinary income, precipitating a sharp drop in multifamily production. In addition, the act placed a cap for the first time on state authority to issue tax-

Almost all direct federal spending is targeted at renters (Fig. 10). Today, the stock of directly subsidized rental housing receives a combination of project-based and tenant-based assistance. Federal resources produce new affordable housing and pay for the maintenance of housing built under programs that have since been discontinued.

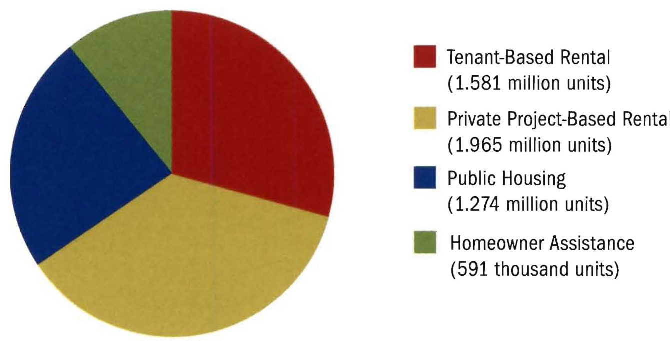
The inventory of privately owned subsidized properties consists of units produced under a variety of programs (Fig. 11). Today, however, none of these programs still produces new units except for the elderly (Section 202) and disabled housing programs (Section 811), which provide capital grants and rental assistance for housing built by nonprofit sponsors, and the Section 515 program, which produces housing in rural areas.

Some of the same tools used to stimulate housing production and preservation are used to foster community development. State credit agencies (usually state housing finance agencies), which administer the LIHTC, typically award points through a competitive process to projects that support broader community development goals. Additional tools include the Community Development Block Grant (CDBG), which may be used for neighborhood redevelopment, economic development, and community services, and HOPE VI grants for the comprehensive redevelopment of public housing.

Figures 9 through 11 provide a snapshot of current federal spending on housing. In 2001, tax incentives totaling $121.2 billion made up the majority of federal housing support. The Joint Committee on Taxation estimates the FY 2001 value of the mortgage interest deduction alone at $64.5 billion, benefiting 32.1 million taxpayers.[2] By comparison, direct spending on housing assistance totals $34.9 billion (Fig. 9).

Figure 10

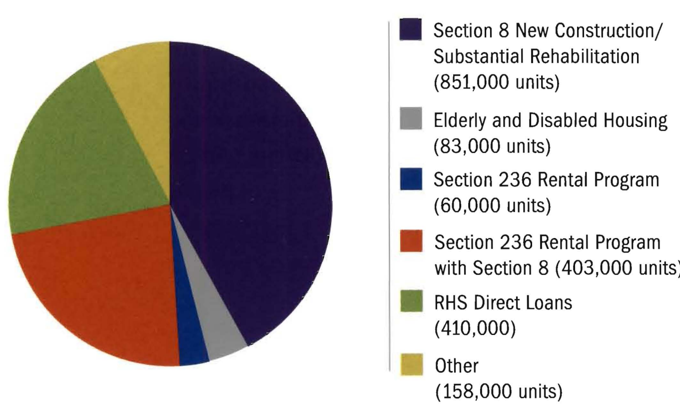
Direct Assistance Primarily Targets Renters and Rental Housing



Source: Appendix 1, Table 3.

Figure 11

The Inventory of Privately Owned Subsidized Properties Totals Just Under Two Million Units



Source: Appendix 1, Table 3. Note: "Other" includes Section 221(d)(3) BMIR, Rent Supplement, Section 8 PD, and remaining Section 8 LMSA units. Units are adjusted to account for overlap among units using more than one program.

Principal Recommendations to Congress

A Framework for Change

The Millennial Housing Commission's vision can be stated quite simply:

to produce and preserve more sustainable, affordable housing in healthy communities to help American families progress up the ladder of economic opportunity.

The Commission's principal recommendations to Congress for achieving this vision are divided into three categories: new tools, major reforms of existing programs, and streamlining of existing programs. The four policy principles of strengthening communities, devolving decision-making, involving the private sector, and ensuring sustainability inform all of the recommendations. The Commissioners believe that these principles will make housing programs work more effectively to attain the goal of more affordable housing in healthy communities, building on what works now to meet bold housing goals tomorrow.

1. **Strengthen communities.**
   The Millennial Housing Commission believes housing policy must foster healthy neighborhoods that form larger communities and function well for residents of all incomes. Housing is, however, only one part of the equation. Good schools, job opportunities, and public safety are also essential to creating healthy communities.

   Distressed inner cites, declining inner-ring suburbs, and booming suburban areas can all benefit from affordable housing that is part of a broader community development plan. In inner cities, safe and well-maintained housing anchors communities, often attracting businesses and additional economic development. In declining, inner-ring neighborhoods, the addition of affordable and appealing housing units can slow—or even reverse—population losses. In high-growth suburban areas, the presence of affordable housing contributes to community by enabling key workers—such as teachers, firefighters, and police—to live near their jobs. Affordable housing also expands the pool of labor to fill lower-wage service jobs, reduces individual commuting times and overall traffic congestion, and allows workers to spend their wages locally.

   People should have the choice to settle in healthy, sustainable communities in any location. To make that possible, the federal government must take the lead in offering states and localities the tools and incentives to encourage development not only of affordable housing, but also of thriving mixed-income communities.

2. **Devolve decision-making to states and local governments, but within a framework of federal standards and performance objectives.**
   While all three levels of government are important players in the housing delivery system, the Commission believes that states—working closely with localities—can best address certain key challenges. It is a major thrust of the MHC's recommendations that Congress pay special attention to assigning appropriate roles and responsibilities to each level of government.

Allowing buildings to fall into disrepair is much more costly in the long run than planning and funding regular maintenance and replacement. Deferred maintenance adds to capital costs over time—each dollar spent on maintenance now is worth many more dollars spent on major renovations later. Housing programs must ensure that resources are available to keep affordable housing in good shape over the long term. All property, whether affordable or not, requires ongoing repairs and capital improvements. Roofing, boilers, and other major systems have limited useful lives. It is a housing policy failure when money is not budgeted to replace major systems in buildings financed and subsidized by the federal government.

Ensuring the long-term sustainability of new affordable units requires a recognition that more durable materials cost more and that sufficient reserves need to be included in the underwriting. At the same time, owners must receive a return on capital that provides sufficient incentive to keep their properties in good repair.

The Commission's principal recommendations are presented below.

New Tools

The Commission proposes several new tools, all of which would be administered by states working with localities. The tools are targeted to unmet need and involve private-sector incentives as appropriate.

Allocate a flexible new tax credit to stimulate production of affordable properties suitable for homeownership.

The federal tax code provides the largest and most often-cited incentive for families to become homeowners—the deductibility of mortgage interest payments and real estate taxes from federal income taxes. For higher-income taxpayers who itemize their deductions, this provision reduces annual tax liabilities and thereby increases disposable income. Most homeowners also benefit from the capital gains exclusion when they sell their principal residences.

Low-income homeowners, however, enjoy few of these tax-related benefits. Because they have smaller mortgages and lower-value properties, these homeowners do not have itemized deductions that exceed the standard deduction. In fact, about 90 percent of the total benefits of the mortgage interest deduction accrue to homeowners with more than $40,000 in income.[1]

To help lift low-income and minority homeownership rates, the MHC recommends creation of a new homeownership tax credit, to be allocated to state housing finance agencies. HFAs would have the flexibility to use the credit to build supply in tighter markets, to stimulate demand where markets are relatively weak, or both.

The advantage of the homeownership tax credit over direct subsidy programs is that it devolves authority to states and relies on private-sector partners to deliver allocated resources. No matter how agencies choose to use the credit, however, the Commission believes it will be a valuable community development resource that enhances the overall stability of neighborhoods.

While a homeownership tax credit is an important additional incentive to create more affordable housing, details of a new credit must be carefully crafted to avoid any adverse impact on the existing Low Income Housing Tax Credit for rental housing.

Enact exit tax relief to encourage preservation.

This is a two-part recommendation that first explains the importance of preservation generally, and then outlines a critical new tool to promote the immediate preservation of at-risk properties.

The Case for Preservation

Broadly speaking, privately owned, multifamily rental units available to low-income families fall into two categories: (1) federally assisted units, in which an owner receives some sort of public, project-based subsidy in exchange for a contractual obligation to maintain affordability for low-income renters, and (2) conventionally financed units, which may be available to low-income renters in some markets but where the owner is without a contractual obligation to maintain affordable rents. Many of the low-income families who occupy conventionally financed units pay more than 50 percent of their incomes in rent.

In 1999, the federally assisted inventory provided one in ten rental units affordable to low-income renter households. For a variety of reasons, units are being lost from both inventories. As part of its strategy to address this crisis, the nation needs to preserve the federally assisted properties and to draw privately held, conventionally financed multifamily units into the long-term affordable stock, where possible.

Losses from the federally assisted inventory. The federally assisted stock generally consists of two types of units: those financed, beginning in the 1960s, with federally subsidized, 40-year mortgages; and those financed, beginning in the 1970s, through Housing Assistance Payment (HAP) contracts between owners and HUD. The HAP contract guaranteed owners a contract rent amount to make up the difference between tenant payments and the fair market rent. In both cases, owners were required to rent to eligible, low-income households for the period of time spelled out in the terms of the federally subsidized financing or contract.

Owners of units financed with mortgage subsidies were permitted, after 20 years, to prepay the remainder of their subsidized mortgages and end their obligation to maintain rents affordable to low-income households. For properties financed through HAP contracts, some contract periods have expired and some remain in effect. When HAP contracts expire, owners can either "opt out" of the program, taking their properties to higher, unregulated market rents, or they can choose to remain in the program. Owners then have the opportunity to enter into multiyear contracts that are, however, subject to annual appropriations.

- ***A new underwriting standard for long-term sustainability.*** All federal programs should embrace a new norm whereby rehabilitated buildings are underwritten to provide 30 years of affordability and newly constructed buildings are underwritten to provide 50 years of affordability. There must be one underwriting standard for each type of building that reflects its respective affordability period. This is a change from the existing system, in which two separate underwriting standards—one for financing and one for affordability restrictions—are in place.

  The best way to ensure a property's long-term physical and financial health is to maintain adequate reserves for replacement. The new underwriting standard must reflect a property's long-term capital needs. The Commission recommends that Congress undertake an analysis of the impediments to establishing and maintaining adequate replacement reserves, including the tax implications.

- ***Efficient use of federal resources, including built-in encouragement of private leverage of public capital.*** The federal system should encourage the use of mixed-income models, the pooling and leveraging of assets, and the creation of economies of scale to reward practitioners who help build efficiencies into the system. There should be built-in rewards and incentives for the quick and efficient use of capital to encourage preservation practitioners to compete favorably with market-rate, private-sector interests.

- ***Recognition of the unique nature and needs of entities committed to expanding the universe of affordable units through preservation.*** The current system forces preservation under an umbrella of affordable housing programs that are geared toward new production. Entities dedicated to preserving currently affordable units and acquiring and then preserving conventionally financed properties must be expressly recognized in U.S. housing policy and programs. The Commission recommends that such "preservation entities" be provided with the tools and resources they need to carry out their unique mission.

- ***Recognition of the broader benefits of preservation.*** U.S. housing policy must recognize that preservation is cheaper than new construction, that the rehabilitation and preservation of units returns the units to low-income families faster than new construction can provide such units, and that maintaining and renovating existing units combats blight and contributes to healthy communities.

The Case for Immediate Preservation via a Preservation Tax Incentive

While these principles must be woven into the overall system for long-term success, the need to preserve at-risk units is immediate and pressing. Because time is of the essence, any proposed tools or approaches that can quickly and efficiently preserve housing should receive heightened attention, support, and funding from the federal government. It is therefore critical that tools such as the proposed preservation tax incentive (PTI) be adopted and enacted as quickly as possible. The PTI would grant exit tax relief to multifamily owners who sell to a preservation entity.

The MHC expects states to use this new tool to address identified need by encouraging private-sector owners of properties to transfer ownership to preservation entities. In the implementation of the recommendation, the Commission envisions different roles for different levels of government, as described below.

Implementation of the Preservation Tax Incentive

Federal role. The Commission recommends that Congress:

1. Specify the minimum required elements of transactions eligible for PTI. For example, Congress may wish to require that the transaction be governed by a "long-term affordable housing use agreement" that specifies ongoing affordability for a certain term. The Commission suggests a minimum use agreement of 30 years and the following affordability requirements:

   - ***For assisted properties:*** The new owner (a preservation entity) must maintain existing federal subsidies. When the affordability period for the existing federal subsidy expires, the new owner may not opt out, must renew at least 50 percent of the federally subsidized units, and must also rent at least 20 percent of the units to households earning no more than 50 percent of AMI or 40 percent of the units to households earning no more than 60 percent of AMI.

   - ***For unassisted properties:*** The new owner (a preservation entity) must make at least 20 percent of units affordable at 50 percent of AMI or 40 percent affordable to households earning 60 percent of AMI. These minimums will ensure that tax credit and tax-exempt bond financed projects will be eligible for relief. They will bring dependable, long-term affordability and a measure of income-mixing to newly preserved buildings.

2. Establish penalties for noncompliance. The Commission suggests the penalty for nonprofits be loss of tax-exempt status; for-profits should pay a tax penalty.

3. Establish broad affordability parameters for newly affordable, preserved units. For example, Congress may wish to specify that a minimum percentage of newly affordable units be targeted to extremely low-income households.

4. Establish general, minimum threshold criteria for an entity to qualify as a preservation entity for purposes of exit tax relief transactions.

5. Clarify that use restrictions, affordability levels, and subsidies can be assumed by other qualified entities.

State role. As described below, states would determine which properties/owners are eligible for a preservation tax incentive. They would also establish specific criteria that define a "preservation entity" and a "preservation transaction":

- ***Criteria for eligible properties/sellers:*** The following types of properties would be eligible for relief: assisted properties with negative tax equity (i.e., properties that, if sold at fair market value, would generate net sales proceeds [over and above debt]

Provide capital subsidies for the production of units for occupancy by extremely low-income households.

The most serious housing problem in America is the mismatch between the number of extremely low-income renter households and the number of units available to them with acceptable quality and affordable rents. This is a problem in absolute terms, with 6.4 million ELI households living in housing that is not affordable. And it is a problem in terms of severity, in that ELI households make up only 25 percent of renters but 76 percent of renter households with severe housing affordability problems. The median ELI household reported paying 54 percent of its income for housing in 1999.

Despite persistent and growing need, it has been more than 20 years since there was an active federal housing production program designed to serve extremely low-income households, other than a relatively small effort to replace housing demolished or otherwise lost from the subsidized inventory. The primary barrier to producing new housing for these families is that the production and operating costs of units for extremely low-income households require rents that exceed the level that they can pay.

To meet the 30-percent-of-income standard, subsidies have to be high enough to cover both capital and operating costs. Thus, even though the need is generally acknowledged, the costs are formidable and require multiyear federal expenditures. Although existing programs (especially Section 8 vouchers, Section 202, and Section 811) provide useful vehicles for addressing ELI housing needs, their funding levels are sufficient to do little more than maintain the status quo. As a consequence, several sources of subsidy are often required to serve such households.

The Commission recommends that Congress address the housing needs of extremely low-income households, as presented in the section on America's housing challenges, through a 100 percent capital subsidy for construction, rehabilitation, or acquisition of units earmarked for extremely low-income households. This new tool would be a substantial state-allocated capital source that would eliminate the need for debt on units, which would be located primarily in mixed-income developments or neighborhoods. Rents on the units would cover operating expenses, including an adequate reserve. The Commission recommends that states work with localities to specify in a state allocation plan how this new capital subsidy tool would be used to address areas of greatest need for additional ELI production in conjunction with other production resources.

The goal of this program is to increase significantly the number of good-quality rental units for ELI households, particularly the number of units located in low-poverty neighborhoods and accessible to employment. Under this proposal, rent levels would cover operating costs—including vacancy losses and adequate replacement reserves—with a reasonable margin for sustainability.

The MHC recognizes that, without additional assistance from other programs or sources, rents would exceed the 30-percent-of-income standard of affordability. Nevertheless, rents would

Neighborhood standards. Low-poverty neighborhoods might be defined as all census tracts except Qualified Census Tracts, or as those with a poverty rate below, say, 20 percent. The standards for inner-city areas could differ from those for suburban or rural areas. State credit agencies could have limited flexibility to approve extremely low-income units in developments outside low-poverty census tracts, particularly in gentrifying neighborhoods or those with active revitalization programs under way.

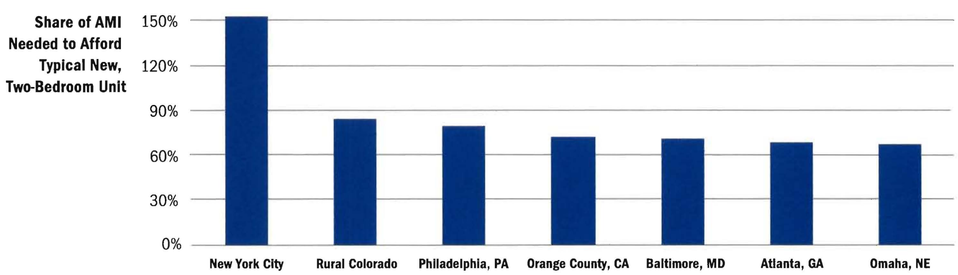
Attract private capital to the production of mixed-income, multifamily rental housing.

The MHC recommends that the limits be taken off states' ability to issue tax-exempt debt for specific multifamily properties, with the condition that eligible properties must restrict rents on at least 20 percent of the units to levels affordable to families with incomes below 80 percent of AMI. The Commission believes that access to credit, at the lowest feasible interest rate, is critical to the production of more housing. In addition, the 20-percent requirement will achieve a degree of affordability without impairing the developer's willingness to participate and will ensure that the program helps to offset the decline in rentals affordable to low- and moderate-income working families (Fig. 12).

The Commission also recommends that states have the flexibility to place rent restrictions on more than 20 percent of the units and to apply deeper targeting to the rent-restricted units, or both. This program is viewed by the Commission as both a production and a community development tool.

Figure 12

Lower-Income Renters in Many Areas Cannot Afford Newly Constructed Apartments



Source: Charlie Wilkins, *Financial Modeling Summary*, prepared for the Millennial Housing Commission, 2001.

Unfortunately, the many silos of categorical programs create almost insurmountable barriers to execution of comprehensive local programs. Federal funding flows to different jurisdictions, on different timetables, with unique planning, performance standards, eligibility determinations, and procurement requirements. Often these requirements are not only incompatible, but they also discourage comprehensive strategies altogether because of the time and energy required.

Funding childcare, employment and training, and enhanced transportation in connection with a housing development may involve four of five agencies with completely separate administrative structures derived from the federal authorizing statutes. The delays and barriers in assembling the desired set of resources drive up costs and discourage private-sector investment in the projects. Private investors gain confidence from well-executed, on-time performance. Such a standard is almost impossible to achieve when navigating the labyrinth of program requirements one at a time.

When state and local leadership overcome these unnecessary barriers, however, the results speak to the value of facilitating such approaches. Comprehensive community initiatives around the country—including Bethel New Life in Chicago, Community Building in Partnership in Baltimore, and the Dudley Street Neighborhood Initiative in Boston—confirm the enhanced return when public investments reinforce each other and attract private-sector investment.

The Commission believes that state and local leadership should have the tools to respond in a highly coordinated fashion to locally unique, comprehensive development proposals. The goal is prompt, consolidated review that crosses program boundaries, and streamlined administration so that private and public energies are not drained by conflicting, overlapping, and duplicate demands for information.

The Commission recommends creation of a new, more potent community development tool that builds on the lessons of successful projects while unifying funding and regulations. This proposal would allow state governors to reserve up to 15 percent of their federal block grant funds (including TANF, CDBG, HOME, Workforce Investment Act (WIA) funds, Social Services Block Grants, Child Care Block Grants, and transportation funding) to support comprehensive redevelopment projects sponsored by local governments, including consortia of local governments in rural areas.

Localities wanting to undertake such projects would apply to the state for funding through programs already administered at the state level. A consolidated program review and decision/award process for all identified programs would follow. The locality could also earmark 15 percent of the funds it receives directly from the federal government for these initiatives. Indeed, one of the factors a governor should consider in approving a request is whether the locality is willing to use its own funds to support the undertaking.

Major Reforms to Existing Programs

Several housing programs are in need of major reform. In particular, public housing and the Federal Housing Administration require significant reconfiguration to align these programs with their stated missions. In addition, the elimination of homelessness is within the nation's reach; the Commission's recommendations are meant to make this goal a reality. Finally, the MHC draws lessons from some of the successes to date of welfare reform, recommending the elimination of rules that can create disincentives to work.

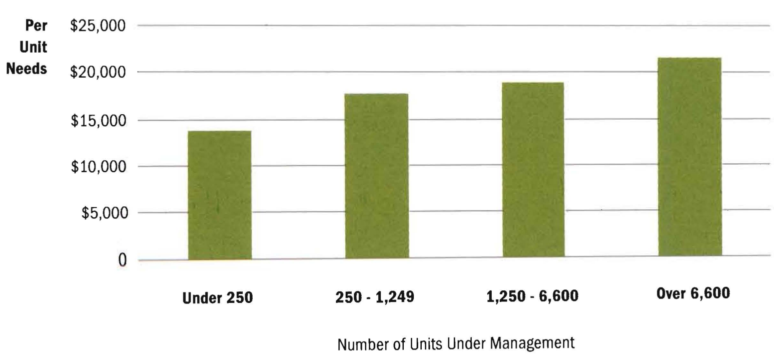
Transform and revitalize the public housing program.

Public housing currently serves 1.3 million of the nation's lowest-income families and elderly and disabled persons. Over time, however, the program has become highly regulated and rule-bound—often serving as a laboratory for a wide, and sometimes contradictory, variety of social and philosophical ideas emanating from well-intentioned laws that have created more problems than they have solved.

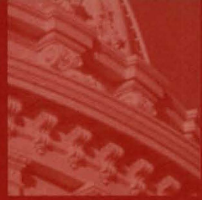
The public housing authorities (PHAs) that administer the program find it increasingly difficult to meet their basic mandate while complying with the maze of regulations. The complexity and cost of compliance not only undermine the effectiveness of the best agencies, but also provide a convenient excuse for the operational failures of the least competent ones. Very small (usually rural) PHAs are particularly burdened, because they must abide by the same statutory and regulatory requirements as large, complex urban agencies but without the means—or the need—to do so.

Figure 13

Large Public Housing Authorities Face the Greatest Modernization Costs



Source: Meryl Finkel et al., *Capital Needs of the Public Housing Stock in 1998: Formula Capital Study*, prepared for the U.S. Department of Housing and Urban Development, January 30, 2000.



- ***Assess the capital, operating, and asset and property management needs of each property***[12] in the public housing inventory to determine the best debt and reserve structure. The first properties to convert would be those in the best condition and locations.

- ***Set up each property as an individually owned entity,*** with its assets outside the public housing Annual Contributions Contract (ACC) between the PHA and HUD. While the entity could be a subsidiary nonprofit corporation of the public housing authority, its assets would have to be freestanding to facilitate debt financing of capital improvements.

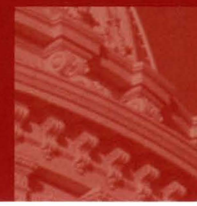
- ***Establish clear and widely accepted standards for redesign,*** unit and site amenities, and physical condition so that the properties are attractive to the full range of eligible families. Such standards would serve to reduce the concentration of the very poorest families in public housing.

- ***Upon turnover, permit PHAs to admit a percentage of market-rate tenants***[13] to properties where income-mixing is feasible. Use of tenant-based subsidies in areas with inadequate supply, or project-based subsidies for units in other locations (to replace the former deeply subsidized public housing units), will also help to retain affordable housing for extremely low-income families.[14]

- ***Replace the Annual Contributions Contract with a Housing Assistance Payment (HAP) contract*** as each property moves to the project-based assistance model. This would immediately reduce the regulatory burden of the PHA and HUD oversight requirements. Properties that cannot or choose not to seek project-based assistance would move to a housing choice voucher-type HAP contract. HUD's public housing oversight structure would ultimately be eliminated.

- ***Use a Section 8 administrator to avoid conflict of interest*** if the PHA is the owner/manager, sets rent levels, and performs housing quality inspections. Such arrangements already exist in many jurisdictions.

- ***Involve the residents in future planning about the project.*** Neither public housing nor other rental housing is truly viable if residents and managers are unaware of or unwilling to consider each others' desires, opinions, and goals. Successful conversion of the public housing stock requires the involvement and support of residents in the planning process as well as in carrying out the transition. Throughout this process, input and participation from public housing residents and other important stakeholders should be actively sought and considered. Residents should have access to the training and technical assistance necessary to make their involvement informed and productive.



command after renovation. Additional credit enhancements or other HUD guarantees would be necessary in that, by definition, the property's condition will require financing that exceeds its market value.

If a PHA decides not to replace or rehabilitate a property, rents would be based on market value, and replacement reserves would continue to accrue. While some public housing properties need no new capital investment, others are in such poor condition or are so poorly located that they do not warrant additional investment. These properties are good candidates for demolition and replacement with vouchers or hard units, depending on input from community stakeholders, including public housing residents, as well as analysis of local markets and housing conditions.

A debt financing strategy has several merits. The long-term costs of this capital improvement approach would likely be lower than the current approach. An added benefit is that improvements can occur quickly, before properties deteriorate further. Finally, debt financing provides another level of operational oversight from lenders, thus substituting standard real estate practice for HUD oversight and regulations.

Debt financing is not, however, appropriate in all cases. For small properties, the ratio of transaction costs to overall debt makes this type of financing impractical. A more suitable approach for these properties would be to use existing capital grant programs or to front-load direct grants.

For properties whose capital needs require rents substantially above market-based levels or Section 8 fair market rents, the alternatives include:

- Using the HOPE VI program to revitalize properties that are well located but in poor condition or otherwise obsolete, and
- Granting PHAs full access to all housing development vehicles including debt financing and tax credits, as well as new loan and grant programs.

While these alternative approaches may add to the already tight competition for tax credits, the ability to compete successfully depends on the credibility of the PHA and its partners as asset and construction managers. Over time, such competition would help integrate public housing into the rest of the affordable housing delivery system and subject PHAs to the same degree of private-sector discipline as owners of tax credit properties. This suggests that Congress should consider an increase in the allocation of the Low Income Housing Tax Credit so that this resource can be used to revitalize the public housing stock without diminishing its availability for other uses.

Finally, the Commission suggests that Congress direct HUD through FHA to work with the private sector and bond-rating agencies to structure a guarantee based on the proposed Section 8 project-based appropriations. Such a guarantee would enable PHAs to leverage private-sector investment for constructing or rehabilitating units affordable to voucher holders and located in mixed-income developments.

Another approach would set rents at 30 percent of income for the first year and then "step up" the level every year thereafter. This again creates an incentive to seek economic opportunity, but gives families a full year to access services and achieve some stability.

6. **Exempt small PHAs from unnecessary and burdensome reporting requirements.**
   Small PHAs must abide by most of the same statutory and regulatory requirements developed for large PHAs. The MHC recommends that PHAs with fewer than 250 units have a simplified contract that establishes basic standards for physical conditions and operations, but strictly limits paperwork and reporting. In this way, small PHAs can appropriately focus their staff and financial resources on property management. Even under these simplified requirements, however, some PHAs that are geographically isolated or face high staff turnover will need ongoing, reliable technical assistance.

Revitalize and restructure the Federal Housing Administration within HUD.

Revitalizing and restructuring the Federal Housing Administration is an urgent priority. FHA multifamily insurance is an indispensable tool for stimulating housing production, and FHA single-family insurance is vital for expanding homeownership among low-income families and minorities. In FY 2001, FHA endorsed more than $100 billion in mortgage insurance under its single-family and multifamily programs, and injected about $4 billion into the federal budget.[19] Indeed, unlike most federal programs and agencies, FHA is a moneymaker.

The potential of FHA to support the production and preservation of affordable housing is hampered, however, by its structure and the prescriptive statutes under which it operates. For example, although federal regulators of financial institutions are permitted to pay salaries above normal federal pay scales in recognition of the special skills demanded by sophisticated financial market operations, FHA's hiring authority is limited by statute and congressional appropriations. FHA's dependence on the appropriations process (instead of its own "earnings"), together with competition for funds within HUD, has led to under-investment in productivity-enhancing technologies that not only makes it difficult for FHA to work efficiently with its industry partners, but also increases operational risk (i.e., risk of managerial shortcomings).

The statutes and regulations dramatically increase the time necessary to develop and implement new products, keeping FHA from being fully responsive to the evolving marketplace. The nature of the political process often leads to highly specific—and sometimes contradictory—changes to programs, further curbing flexible implementation.

1. **Restructure FHA as a wholly owned government corporation within HUD.**
   A corporate structure would give FHA maximum flexibility to adapt its programs to the evolving finance market without relying on Congress to legislate each change. This could be accomplished with no substantial budget impact.

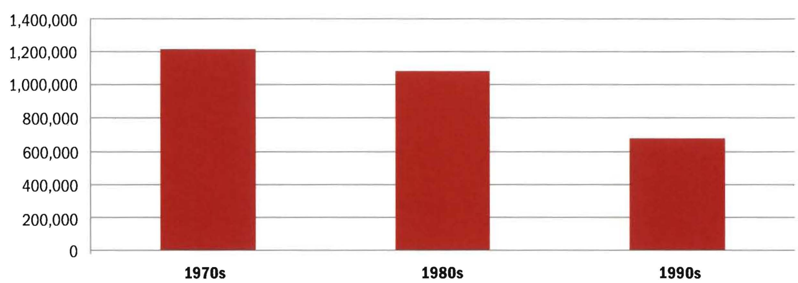
With this new structure, FHA could invest in technology to improve its efficiency and reduce its risk, thereby creating production and ownership opportunities that would otherwise not exist. A corporate structure would also serve to attract staff with the requisite skills and experience to manage FHA's nearly $500 billion mortgage insurance program. Equally important, however, FHA would remain an integral part of HUD and, as such, an effective force for the production and preservation of affordable housing.

2. Provide for more flexible multifamily operations.

Statutory reforms are needed to grant FHA a sufficient degree of flexibility to improve its multifamily operations (Fig. 14). Although the Commission recommends the following changes be made as part of a restructured FHA, they would by themselves improve FHA's support of multifamily housing. At minimum, Congress should pass statutes that:

Figure 14

The Number of FHA-Insured Multifamily Units Continued to Fall in the 1990s



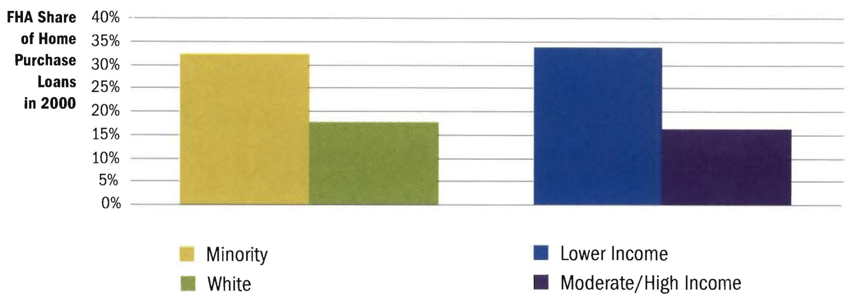
Source: U.S. Department of Housing and Urban Development, Office of Multi-Family Housing, April 2001.

- ***Combine all multifamily programs in the General Insurance and Special Risk Insurance (GI/SRI) Fund into a single program*** for purposes of determining credit subsidy allocations. As currently structured, any individual insurance program that does not break even requires an appropriation of credit subsidy from Congress, even if other programs within the fund generate earnings. When the subsidy runs out, these programs must shut down for the remainder of the fiscal year unless Congress makes an emergency appropriation. A single appropriation of credit subsidy for all programs in the GI/SRI fund would eliminate this problem. Enabling FHA to manage its multifamily programs as a single fund would allow it to set premiums and target loan volumes for each program in such a way that the fund as a whole requires no appropriation of budget authority.

- ***Permit FHA to vary the terms or other aspects of its multifamily insurance programs.*** Today, program specifics are spelled out in statutes that require congressional legislation to change. Broader authorities should replace many of these details. In crafting such legislation, Congress can look to its own FHA multifamily risk-sharing legislation, which gives FHA the flexibility to react to market changes and other conditions much more rapidly.

Figure 15

FHA Is Critical to Minority and Low-Income Homebuyers



Source: Home Mortgage Disclosure Act, Community Reinvestment Act data, 2000.

While FHA can absorb risk better, potential partners may have superior risk assessment and management systems. Others may be able to provide access to new products and delivery systems targeting communities with underserved borrowers that FHA does not yet reach, such as the subprime mortgage market.[23] Congress should establish one FHA risk-sharing program for credit subsidy purposes and allow it to operate both programs that break even and programs that do not within this authority, provided it achieves an overall target.

- ***Authorize FHA to set its own standard for selecting business partners.*** At present, FHA approves lenders, but not appraisers, under congressionally mandated standards. FHA's inability to select appraisers and other business partners on its own terms severely handicaps its capacity to manage risk and, by extension, the risk to communities from liquidating inventories of defaulted loans.

- ***Expressly authorize FHA to introduce new products,*** such as pool insurance products, without requiring Congress to pass a new statute for each. This would offer the same benefits on the single-family side as those described for the multifamily side.

- ***Urge FHA to use sophisticated private-sector techniques to prevent mortgage defaults and, when defaults are unavoidable, reduce their cost.*** While FHA has made progress in loss mitigation and property disposition in recent years, potential partners have demonstrated far greater success in these areas. In 1998, Congress gave FHA authority to take assignment of loans for purposes of transferring them to partners who would manage loss mitigation, foreclosure, and property disposition. The authority also allows FHA to take an equity interest in a joint venture partnership, so that FHA can share in the returns generated from more efficient and effective operations. The Commission recommends that FHA implement this existing authority for defaulted loan sales to joint ventures.

This recommendation is not to suggest that FHA should simply sell its entire inventory of foreclosed homes for the highest price. That approach has had—and would continue

The homeless can be divided into two broad groups. Up to one-third are the "chronically homeless" who experience frequent or long-term episodes of homelessness. This population—primarily single adults, although including a small percentage of families as well—generally suffer health or substance abuse problems in addition to extreme poverty.

Many of these individuals live in the homeless system, cycling from shelters to the streets to jails and hospitals—often at enormous cost. A recent study of New York City's homeless system found that the public cost to care for a homeless, mentally ill person was roughly equivalent to the cost of housing that same person.[28] The chronically homeless require "permanent supportive housing" to escape homelessness and reduce the enormous burden on public care systems.

The "transitionally homeless," in contrast, are households whose predominant need is rapid access to affordable housing. Overall, the transitionally homeless have more in common with the "housed poor" than with the chronically homeless. In fact, many of the needs of the transitionally homeless can be met by increasing the affordable housing supply for extremely low-income families, as well as by policies promoting employment and self-sufficiency.

The MHC strongly endorses a program to end chronic homelessness within 10 years through provision of additional supportive housing. Best estimates put the number of chronically homeless people near 200,000 and the number of appropriate units near 50,000. This shortfall calls for another 150,000 units of suitable housing over the next 10 years, along with continued funding for the 50,000 or so existing units.

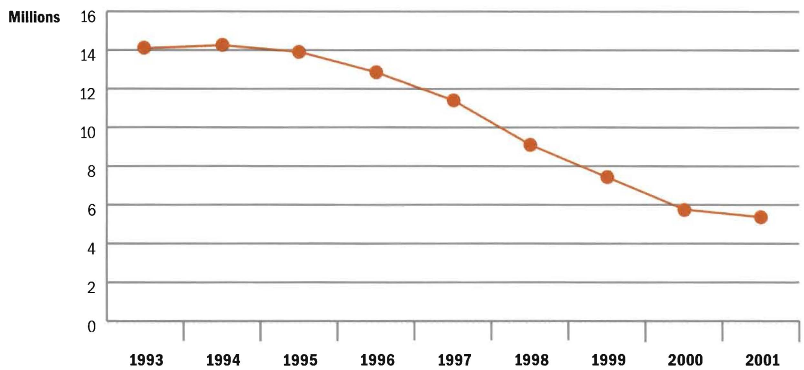
The tools to achieve this goal are already in place. For the last three fiscal years, 30 percent of HUD McKinney-Vento Homeless Assistance funding has been set aside for permanent housing through the Shelter Plus Care, Supportive Housing, and Single Room Occupancy programs. The Commission recommends that this set-aside be made permanent as a way to ensure the addition of 15,000 incremental units of permanent supportive housing each year.

A related recommendation is to transfer renewal funding for expiring rent and operating subsidies for permanent supportive housing (initially funded under McKinney-Vento) to HUD's Housing Certificate Fund. This would treat HUD-supported housing for the homeless similarly to other HUD-subsidized housing, freeing current year McKinney-Vento appropriations for investment in incremental permanent supportive housing units and other initiatives for the homeless.

Together, these two initiatives would serve to end chronic homelessness within 10 years. Policies recommended elsewhere in this report would also greatly reduce transitional homelessness. Moving these populations out of shelters and jails and off the streets is in the best interests not only of housing policymakers but of all Americans.

Figure 16a

Welfare Caseloads Have Dropped Sharply Since Welfare Reform

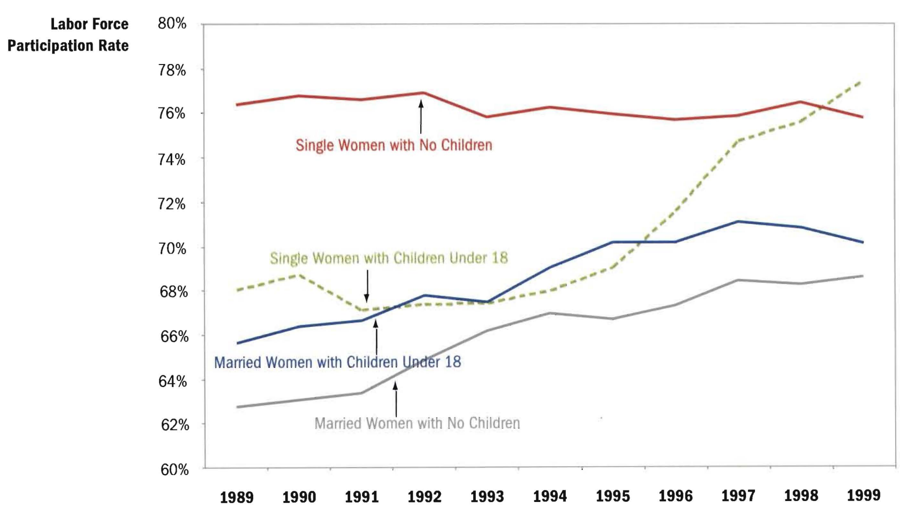


Source: Department of Health and Human Services, Administration for Children and Families, April 2002.

Since enactment of welfare reform and creation of Temporary Assistance for Needy Families, many states have made substantial changes to the provision of family assistance. The TANF law encouraged states to link assistance with work requirements. The combination of federal welfare reform, state flexibility in implementation, and economic expansion has led to a dramatic decrease in the number of AFDC/TANF-assisted households and a simultaneous increase in the percentage of TANF-assisted single mothers participating in the workforce (Fig. 16b).

Figure 16b

Employment Among Single Mothers with Children Has Skyrocketed



Source: Rebecca M. Blank, "Declining Caseloads/increased Work: What We Conclude About the Effects of Welfare Reform?" Federal Reserve Bank of New York, *Economic Policy Review*, September 2001.

physical or mental illness and families making the transition from welfare to work. In certain circumstances, vouchers can also be used to help families become homeowners.

Because the program is flexible, cost-effective, and successful in its mission, the MHC believes housing vouchers should continue to be the linchpin of a national policy providing very low-income renters access to the privately owned housing stock.

The MHC recommends appropriation of additional funds for substantial annual increments of vouchers to address the housing problems of extremely low- and very low-income families who lack access to other housing assistance. The MHC also supports expanded use of vouchers for homeownership to help low-income families build assets. Finally, the MHC recommends specific refinements that would increase the program's efficiency and effectiveness.

1. **Improve utilization and success rates.**[30]
   HUD needs to diagnose the reasons for the limited success of the voucher program at some PHAs and offer targeted technical assistance.[31] Voucher units should be reallocated from low-utilization PHAs to entities serving the same geographic area and households. Where reallocation is not feasible, the PHA could be required to contract with another entity to administer the unused vouchers. In all cases, households on the original PHA's waiting list should have priority for the unused vouchers.

   HUD could also make two simple administrative changes that would improve the voucher system in tight rental markets: (1) expand the resources devoted to rent surveys so that published Fair Market Rents do not lag actual rents, and (2) quickly approve exception payment standards when census data demonstrate that average area rents are at the level of the exception sought (with some appropriate upper limit).

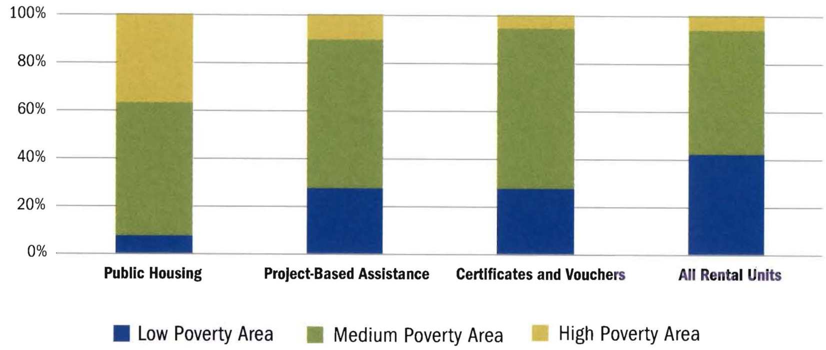
2. **Increase landlord participation.**
   HUD and PHAs should develop consensus standards for shortening the inspection and lease approval process and for providing better service to landlords. These standards should be based on a review of PHA performance, feedback from both landlords and voucher holders, and review of all standards that affect landlord participation, such as lease approvals, inspections, and voucher transfer payments.

   The MHC also recommends that HUD provide technical assistance to PHAs for improving landlord participation, disseminate best practices information to program administrators, experiment with giving PHAs greater flexibility in applying the Housing Quality Standards (HQS) to attract owners to the program, and change the cap on the family rent contribution for newly rented voucher units to 40 percent of gross (rather than adjusted) income.[32]

3. **Link vouchers to housing production programs.**
   The MHC recommends that HUD strengthen and enforce the requirement that owners of housing produced under federally funded programs accept households with vouchers. This is in an effort to enable extremely low-income families to live in rental housing produced with other subsidy sources that would otherwise be unaffordable.[33] In the interests of

Figure 17

Housing Choice Vouchers Help Recipients Move to Lower Poverty Areas



Note: Low poverty areas defined as tracts having under 10% of households at or below poverty level; medium poverty areas as having 10-39% of households at or below poverty level; and high poverty areas as having over 40% of households at or below poverty level.

Source: Sandra J. Newman and Ann B. Schnare, "'...And a Suitable Living Environment': The Failure of Housing Programs to Deliver on Neighborhood Quality," *Housing Policy Debate* 8:4, 1997.

5. Link vouchers to non-housing programs.

HUD should allow other agencies to compete for special allocations of vouchers for certain populations, but require that PHAs (or regional consortia of PHAs) perform key operations such as housing inspections, rent-setting, and payments to landlords. HUD should monitor performance of these functions as part of the PHA's overall voucher program.

Housing vouchers can also work effectively with other types of assistance programs for special-needs populations. In particular, as states expand community-based housing options, they are likely to look increasingly to vouchers to provide permanent housing supports for persons with disabilities. This will require establishing stronger partnerships between PHAs and other providers of supportive services, and permitting state agencies and nonprofits to administer special-purpose vouchers.

6. Allow for the flexible use of Section 8 project-based units.

In addition to expanding tenant-based housing choice vouchers, the Commission proposes certain improvements to the project-based Section 8 program. More than 800,000 units of project-based Section 8 units are still in the federally assisted stock. While most are in good condition, some are obsolete, deteriorating, and located in areas where assisted housing is highly concentrated. Others are at risk of opt out from their Section 8 contracts.

Unfortunately, the treatment of project-based Section 8 units is rather inflexible. Current HUD policy does not appear to allow the transfer of subsidies from deteriorated properties to other locations to create replacement housing. Although the Mark-to-Market program

The LIHTC is administered by state credit agencies (usually state housing finance agencies). Federal program guidelines are spelled out in the Internal Revenue Code (IRC). Through the IRC, the federal government defines tenant income and rent restrictions, generally describes the Qualified Allocation Plan (QAP) process that credit agencies must use in awarding credits to projects that propose to serve such tenants, outlines the eligible project costs for which the credit may be used, explains how investor benefits relate to eligible project costs, and lays out compliance requirements for investors.

Credits are allocated annually to state credit agencies on a per capita basis. The agencies then award credits to individual developers via the state-developed QAP, which identifies statewide housing needs and lays out the agency's ranking factors given those needs. Allocators have enormous flexibility in designing their QAPs. In effect, through its QAP requirement, the federal government mandates that state credit agencies define the public benefit to be achieved through the use of the tax credit, which is essentially a public subsidy.

Developers who compete successfully for a credit allocation then sell their credits to private-sector investors, with proceeds of the sale providing project equity. Investors derive economic return as long as the property remains in compliance for the required period of time. The statute requires a 15-year initial compliance period and mandates an extended-use agreement under which properties must continue to serve low-income tenants for an additional 15 years, but with a contingency clause that allows for conversion to market rate under certain conditions.[36]

Enacted in the National Affordable Housing Act of 1990, HOME is a federal block grant program administered by the U.S. Department of Housing and Urban Development. Grants are allocated annually, by formula, to states, localities, and consortia of local governments. The federal government determines the allocation formula, sets overall program objectives and eligibility requirements for applicants and beneficiaries, and defines eligible and ineligible uses of the funds. Beyond that, HOME fund beneficiaries have great flexibility to determine how best to use the funds to meet local needs (Fig. 18).

In addition to expanding the supply of affordable—particularly rental—housing for low- and very low-income families, one of the stated national objectives of the HOME program is to "strengthen the ability of state and local governments to design and implement strategies for achieving adequate supplies of decent, affordable housing."[37] Funds can also be used for capacity-building assistance to beneficiaries, and to strengthen partnerships between beneficiaries and the private sector.

Both LIHTC and HOME have helped to build the capacity of state and local jurisdictions to engage in housing development. The LIHTC in particular has imposed private-sector discipline on state credit agencies and developers who benefit from tax credit equity, because private-sector investors in LIHTC-funded projects face severe tax penalties should the projects fail to comply with IRC requirements. State credit agencies are required to monitor projects' physical condition and compliance with federal tenant and rent restrictions, so private-sector investors demand effective public oversight of the projects, otherwise they risk losing the

1. **Improve the Low Income Housing Tax Credit Program.**
   - ***Allow sponsors of tax credit properties in low-income rural areas to set rent caps based on statewide median income.*** This recommendation is intended to facilitate use of the tax credit in rural areas where the median income is too low relative to construction costs to stimulate multifamily housing production. The proposed change would allow states to extend eligibility, where appropriate, to developments whose rents are affordable based on statewide (rather than countywide) median incomes. Additional subsidies will be necessary to make an appropriate portion of the units available to extremely low-income families.

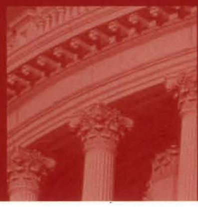
   - ***Remove impediments to the use of tax credits for preservation.*** Repealing IRC §42(d)(2)(B)(ii) would make it easier to transfer desirable tax credit properties to preservation entities. This "anti-churning" provision precludes a property from receiving an allocation of acquisition tax credits if it has changed hands within 10 years. The 10-year rule was put into place to prevent owners from selling or transferring properties in order to gain tax benefits. Because Congress has since eliminated or restricted these tax benefits, the 10-year rule is now obsolete.

   - ***Remove the prohibition against combining LIHTC with assistance under the §8(e)(2) moderate rehabilitation program.*** IRC §42(c)(2)(B) precludes a moderate rehabilitation property from receiving an allocation of tax credits. This prohibition was imposed because of concerns about inappropriate awards of assistance in the early 1980s. The overriding concern today, however, is the need to preserve affordable housing for long-term affordable housing use. Repeal of this provision would support this goal.

   - ***Clarify what project costs can be included in eligible basis.*** Ambiguity about what costs may and may not be included in eligible basis is a fundamental problem in the development and financing of tax credit properties. Five Technical Advice Memoranda issued by the Internal Revenue Service (IRS) in late 2000 in response to confusion over the eligibility of particular costs resulted in IRS positions contrary to common industry practice. The Commission recommends that Congress provide needed clarity on this issue.

2. **Improve the HOME Investment Partnerships Program.**
   - ***Given the widely recognized success of the HOME program, enact a substantial increase in HOME funding for both states and local jurisdictions.*** In addition, the Commission recommends raising HOME's minimum state funding level from $3 million to $5 million, with the increase in the minimum funding level coming from the overall state portion of the substantial increase recommended above. This minimum funding level increase would affect allocations to 12 states.

   - ***Allow the use of HOME funds to capitalize a long-term project reserve account.*** Under current regulations, HOME funds may be used to capitalize an initial operating deficit reserve to meet any shortfall during project rent-up. Long-term reserves, in contrast, are the only cost for which a developer must secure private debt, which complicates the process of financing HOME projects. The Commission recommends that



- ***Allow a "basis boost" for tax credit developments in high-poverty, high-cost areas, even when they also receive HOME assistance.*** This recommendation would eliminate a barrier to using the credit for new development or substantial rehabilitation in high-poverty areas where development costs are high relative to AMI. To encourage use of the tax credit in such areas, current law provides for a "basis boost" of up to 30 percent for tax credit properties. The statute, however, makes developments using HOME funding ineligible, effectively discouraging use of the tax credit. It should therefore be eliminated.

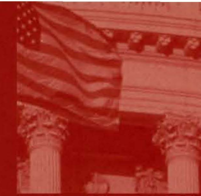
- ***Delegate subsidy-layering reviews for tax credit properties to state allocating agencies.*** Section 102(d) of the Department of Housing and Urban Development Reform Act of 1989 requires the Secretary to certify that HUD assistance to any housing project is no more than necessary to make the project feasible, taking into account other forms of assistance. Section 911 of the Housing and Community Development Act of 1992 specifies that this requirement for projects receiving HUD assistance and tax credits can be satisfied by certification from the housing credit agency to the HUD Secretary, within certain guidelines. IRC §42(m)(2) requires allocating agencies to assure that the amount of credit allocated to a project is no more than is needed. The Commission therefore recommends repeal of §102(d) and §911, as well as delegation of the subsidy-layering review to state allocating agencies. Congress may wish to direct these agencies to certify to the HUD Secretary that subsidy use meets agreed-upon guidelines.

- ***Allow states to use Temporary Assistance to Needy Families (TANF) funds for one-time grants to existing tax credit properties*** without reducing the properties' eligible basis, as long as owners agree to reduce rents for eligible families for an agreed-upon period. IRC §42(d)(5)(A) reduces the eligible basis of a LIHTC building by the amount of any federal funding, thus effectively preventing states from using TANF funds to reduce the debt service and operating costs of such properties. The Commission believes that allowing states the option to make one-time grants from TANF funds in return for deeper targeting and longer periods of affordability would provide important support for former welfare recipients.

Expand states' ability to use the Mortgage Revenue Bond program.

Subject to various restrictions, state housing finance agencies typically use the proceeds from Mortgage Revenue Bond (MRB) issues to generate additional mortgages. Initially, HFAs could use all the payments from MRB-financed mortgages to issue new mortgages. In 1988, however, HFAs were required to use principal payments received after 10 years from bond issuance to pay off the bonds. This now-obsolete requirement was enacted when the MRB program faced an imminent sunset.

The mortgage volume lost due to the 10-year rule has been significant. Losses over the last four years have totaled nearly 109,000 mortgages. Through 2005, the 10-year rule is expected to result in additional lost mortgage volume of about $2 billion to $3 billion—or upwards of 27,000 mortgages—annually (Fig. 19).[38]



The Commission also makes the following recommendations to address issues related to other restrictions on MRBs.

1. Given enforcement of income limits, remove the limits on the purchase prices of homes financed. Purchase price limits were enacted when the program had no income limits. Currently, underwriting standards combined with income limits in effect amount to appropriate purchase price limits.

2. Given enforcement of income limits, repeal the first-time homebuyer eligibility requirement so that low-income owners who need to sell and relocate to take advantage of employment or other opportunities can still benefit from the program. The Commission recommends that Congress consider permitting states to adopt rules beyond the current recapture provision to ensure that repeal of the first-time homebuyer eligibility requirement does not result in windfalls to sellers of properties financed under the program that have appreciated significantly.

3. For states that issue Veterans Mortgage Bonds, remove restrictions limiting eligibility to Veterans who were "on active duty before January 1, 1977, and applied for financing within 30 years of being on active duty."

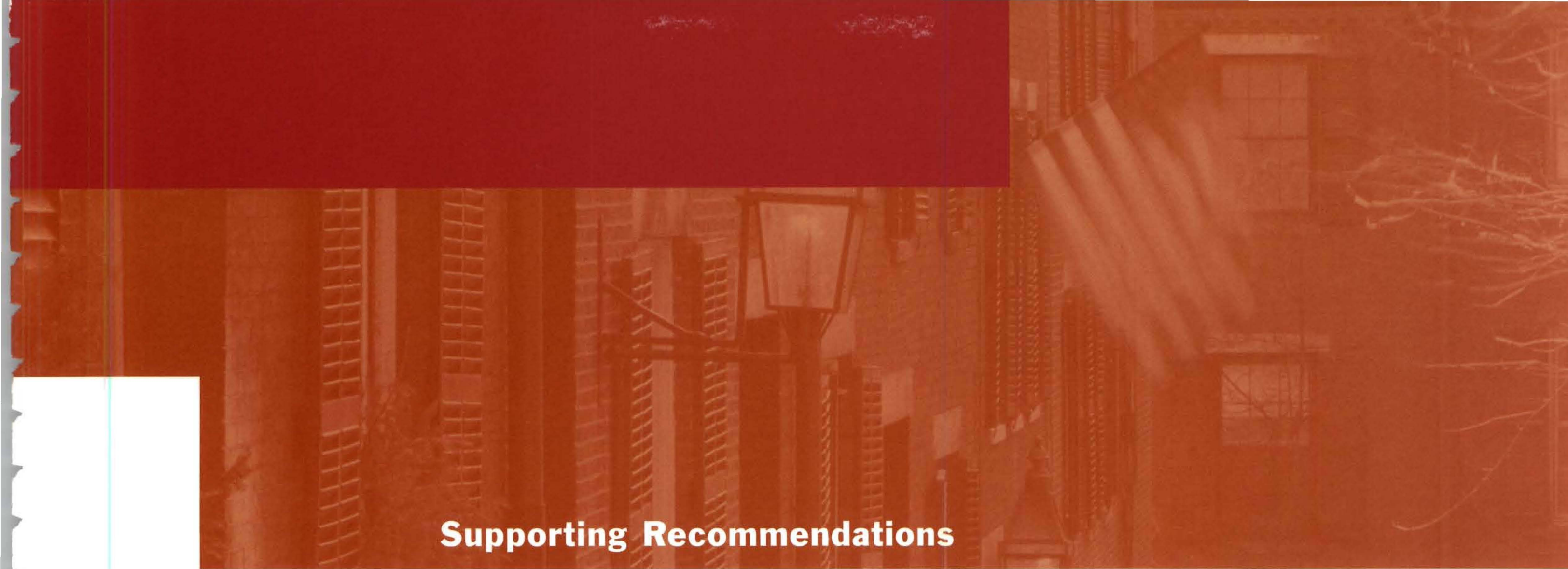
4. Increase the limits on MRB home improvement loans to the FHA Title I loan level.

Revise federal budget laws that deter affordable housing production and preservation.

Budget laws inhibit HUD—as well as other government departments and agencies—from entering into contracts requiring more than one year's funding. In the case of Housing Assistance Payment (HAP) contracts, this restriction has led to the introduction of language in multiyear contacts that subjects HUD's payment obligation under the agreement "to the availability of sufficient appropriations."

This language, known as the "HAP condition," essentially transfers the appropriations risk to owners and lenders. This added uncertainty about payment encourages owners either to remove their properties from the affordable stock or to defer needed maintenance and repair. Lenders predictably protect themselves against this risk by avoiding such properties, requiring reserves, and/or making smaller loans at higher rates with more stringent terms.

The HAP condition thus discourages private-sector investment in affordable housing, but without in any way reducing federal expenditures or obligations. Appropriations for housing assistance under Section 8 have never been—and are unlikely ever to be—decreased. Even if the HAP condition were exercised, the government would still be obliged to provide resources to manage the transition from project- to tenant-based subsidies. Thus, while the HAP condition is largely meaningless, neither owners nor lenders view it as such.



Supporting Recommendations

The Millennial Housing Commission presents the following supporting recommendations.

Increase funding for housing assistance in rural areas.

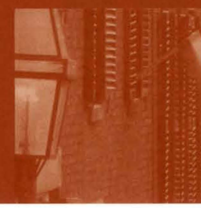
By definition, rural areas are both remote and lightly populated. Many small town and farming communities were bypassed in the recent good economic times. As a result, poverty rates, unemployment rates, and the incidence of housing problems are at levels approaching those of the nation's big cities.

But rural housing needs are harder to serve than most urban needs, and are often neglected by major federal housing production programs such as HOME, CDBG, and the Low Income Housing Tax Credit. As a result, the Rural Housing Service (RHS) programs of the U.S. Department of Agriculture have been the primary source of rural housing assistance since 1949.

In addition to underfunding, rural areas face unique housing challenges. In particular, homeownership is the predominant tenure in rural areas, and there are far more owners than renters with affordability problems. Moreover, housing vouchers often do not work because there is not enough supply from which to choose.

In recent years, federal spending on rural housing programs has been dramatically reduced. As a result, few new housing units have been added in the poorer, more remote rural areas that the Department of Agriculture has historically served. There is substantial demand and need for rural housing assistance, and backlogs for loans are at historic highs. The Commission believes that federal rural housing programs are an important element of the nation's housing finance and delivery system, and that Congress and the Administration should therefore increase appropriations for low-income housing in rural America.

Specifically, the Commission recommends that Congress provide adequate funding for core RHS housing programs, including Section 515 rental housing, Section 521 rental assistance and housing assistance for farm workers, Section 502 homeownership loans and guarantees, and others. It should also ensure that rural areas receive their fair share of resources from other federal production programs based on objective measures of proportionate housing need. States need to pay special attention to the needs of rural areas as they allocate funding through these programs.



5. Develop a demonstration program for the provision of housing for tribal college students and faculty. There are 32 tribal colleges today, most of which are located in isolated areas where housing is in short supply. The American Indian population has become increasingly younger, and college education that is obtainable is critical for improving the self-sufficiency of future generations. Tribal colleges receive little or no funding from state governments.

6. Broaden the ability of tribes to issue tax-exempt private activity bonds for housing. Current law effectively prohibits a borrower in a tax-exempt issuance from relying on future federal financial assistance (e.g., guaranteed payments) to repay the loan. While various exemptions from this prohibition do exist, none is for programs tailored to Indian tribes. Under current law, tribes can issue tax-exempt bonds for rental units owned by the tribe and leased to tribal members, but not for single-family or multifamily units owned by qualified residents. In addition, tribes cannot issue tax-exempt bonds for rental housing owned by a partnership in which the tribe is a member.

Establish Individual Homeownership Development Accounts to help more low-income households buy homes.

An estimated 3.6 million renters are unable to buy homes because they cannot cover the cash outlays needed for downpayment and closing costs.[8] Individual Homeownership Development Accounts (IHDAs) are an innovative way to help low-income families save money for this purpose.

In partnership with the financial industry, an IHDA program would help make homeownership possible for more families. Similar to 401(k)s, these accounts would offer matching funds from private and public sources for each dollar saved. Participants would also receive valuable financial education and counseling. To encourage households to open IHDAs, it might be useful to provide incentives to employers, financial institutions, nonprofits, foundations, and family members to match up to $2,500 in annual IHDA savings.[9] Tax deductions for these matching funds would create additional incentives to participate in the program.

In this spirit, the Commission recommends that the 401(k) and IRA statutes be amended to allow financial institutions to monitor IHDA deposits for Community Reinvestment Act credit. This will encourage institutions to participate in asset-building for account holders in a cost-efficient way since the basic administrative structure is already in place. IHDA program monitors would be responsible for tracking deposits and their use for up to five years, ensuring that families who either violate program terms or do not use their funds pay taxes on a portion of the accrued value.

Undertake a study of the Davis-Bacon Act requirements.

Enacted during the Depression, the Davis-Bacon Act was intended to protect the wages of construction workers. The act requires builders on all federally funded or assisted projects to pay at least the local "prevailing wage" on any construction contract valued at more than $2,000. The prevailing wage is calculated as either the wage that a majority of workers in that craft receive or, lacking a majority, a weighted average of all the wages paid in that craft in the locality.

Evidence presented to the MHC suggests that wage levels set under this procedure are higher than actual wages paid. Clearly, this appears to be a serious issue in at least some parts of the country and for certain types of construction systems. The Commission is concerned about any requirements that raise the cost of housing. At the same time, however, it is aware that Davis-Bacon effectively increases incomes for construction workers, thus enhancing their economic opportunity.

Given the competing viewpoints, the Commission recommends that Congress undertake a study of the Davis-Bacon requirements and make improvements in such areas as the accuracy of the wage data, the applicability threshold, and the reporting requirements.

Address regulatory barriers that either add to the cost of or effectively discourage housing production.

However well intended, regulations may either increase the cost of housing production (making units less affordable) or effectively discourage production. The Commission recommends that Congress consider three approaches for addressing the effects of such regulations.

One approach to removing such barriers, already passed by the U.S. House of Representatives (H.R. 3899), is to require all federal agencies to include a housing impact analysis as part of the rule-making process. The housing impact statement would serve to focus consistent attention on the question of how proposed rules and regulations might affect home prices.

Each housing impact analysis would include: (1) a description of the reasons why action is being considered; (2) a succinct statement of the objectives of, and legal basis for, the rule or regulation; (3) a description of and, where feasible, an estimate of the effects that the rule or regulation would have on the cost or supply of housing or land; and (4) identification, to the extent possible, of all relevant federal rules that may duplicate, overlap, or conflict with the proposed rule or regulation.

H.R. 3899 also reauthorized grants, originally included in the Housing and Community Development Act of 1992, that would serve as incentives for states and localities to develop strategies for removing regulatory barriers. It also required communities to demonstrate a "good faith effort" to remove barriers when they submit their Consolidated Plans to HUD for HOME and CDBG funding. Finally, H.R. 3899 proposed establishment of a clearinghouse

This financing gap not only weighs against the production of smaller, usually urban, rental properties, but it also hampers preservation of existing units. With more than one-third of all rental structures falling within the small multifamily category, providing a strong secondary market for these loans is an important way to preserve and expand the affordable supply. To address this gap, the Commission recommends the following measures:

- Create an FHA small multifamily pool insurance program. Loans for small multifamily properties can be unprofitable because of their perceived risks and the high costs of credit enhancement relative to loan size. The Commission recommends the creation of FHA pool insurance for small multifamily properties to facilitate loan pooling, diversify risk, and reduce credit enhancement costs. Such a program would give local lenders an outlet for small multifamily loans at lower cost than current FHA programs.

- Streamline FHA's existing small multifamily whole loan insurance. Although FHA introduced its Small Project Processing program in the 1990s to increase small multifamily lending, the program has attracted little interest from lenders. The Federal Home Loan Bank (FHLB) of Boston has, however, demonstrated that eliminating unnecessary and costly requirements would increase its usage. FHA should work with the Boston FHLB to make these changes, and reach out to other Federal Home Loan Banks to encourage local banks to originate FHA-insured small multifamily loans.

- Encourage the government-sponsored enterprises and lenders to make loans for small multifamily properties. HUD's affordable housing goals already encourage Fannie Mae and Freddie Mac to make small multifamily loans. The Federal Housing Finance Board may wish to consider similar goals for the Federal Home Loan Banks, while state housing finance agencies could adopt their own goals. The Commission recommends extending small multifamily financing goals to other lenders as a way to direct energies into this market. Congress could also encourage the Federal Home Loan Banks to support multifamily lending through initiatives to make advances on favorable terms.

- Fund national data collection on multifamily lending and promote standardization of lending practices. Relative to loan size, the costs of underwriting and servicing small multifamily loans, as well as making securities out of small multifamily loan pools, are higher than those for large multifamily loans. These high fixed costs could be reduced by improving and centralizing information sources for appraisals, environmental reviews, and loan performance, and by standardizing documents, bankruptcy rules, and title requirements.

  The Commission recommends a national data collection effort to analyze the risks of multifamily lending. While reducing the costs of all multifamily loans, this would especially benefit small multifamily lending. The Multifamily Housing Institute has already made significant advances toward this goal, but progress has stalled because of insufficient funding for startup and operating costs, and because of the uncertain commitment from the government-sponsored enterprises to supply data.

Administration, FHA should offer both individual and pooled construction-only products, working both alone and in tandem with risk-sharing partners to deliver them.

- Grant government-sponsored enterprises express authority to purchase construction-only loans. It is unclear whether the GSEs can purchase construction-only loans. Their charters should therefore be amended to give them explicit authority to do so.
- Require banking regulators to collect data as well as publish sufficiently detailed reports on the activity and performance of real estate loans. Loan activity and performance reports from banking regulators should separate out results for commercial and residential real estate loans. The reports should also provide detail on the three major types of loans—land acquisition, land development, and construction—within these broad categories.

Launch a demonstration project for comprehensive community-based work.

Some neighborhood-based needs and initiatives fall outside the boundaries of traditional federal anti-poverty programs. In addition, government cannot provide all of the funding needed for the intensive community development required.

Private foundations have funded many demonstration projects that combine affordable housing development, economic development, job training, childcare, and transportation projects to improve all systems in a neighborhood at once. The Commission recommends combining the interest and resources of these large philanthropies with funding from the federal government.

This new public-private partnership could be modeled on the National Community Development Initiative (NCDI), a funding collaborative that includes the Department of Housing and Urban Development, major foundations, banks, and insurance companies. NCDI directs funding to community development corporations (CDCs). Three dollars of private foundation money are matched by one dollar of HUD funding in a pool used to improve the community development infrastructure in 23 selected cities. HUD participates equally with the private sector in funding decisions.

Under the new partnership, the Departments of Health and Human Services, Housing and Urban Development, Transportation, and Labor could participate in a pool that would also receive contributions from major foundations. The three-to-one private-sector match would apply. The new partnership would, however, funnel money to a broader set of community-based nonprofits focused on affordable housing development, job training, health care, childcare, transportation, and other appropriate community development activities.

A board composed of representatives of the private foundations and public agencies would make funding decisions. Localities would apply to this board for funding.

way of promoting homeownership among such households, who often struggle to manage consumer debt or need cash for emergencies but are currently prohibited from refinancing. Borrower counseling should be a condition of refinancing or issuance of a second mortgage.

Improve manufactured homebuyer and owner access to capital markets.

Manufactured housing plays an important role in meeting the nation's affordable housing needs. During the 1990s, manufactured housing placements accounted for one-quarter of all new housing starts[15] and, from 1997 to 1999, 72 percent of new units affordable to low-income homebuyers.[16]

The manufactured housing industry has evolved in the last decade to deliver a better-quality product that saves as much as 25 percent of development costs.[17] Indeed, recent innovations in design, including multi-stories and attached garages, make manufactured housing a viable alternative for urban in-fill developments.

Development of an appropriate financing system for manufactured housing has not kept pace with these design and quality improvements. Until very recently, few lenders were willing to finance manufactured homes as real estate, except where land was owned or a land lease was in place that extended beyond the mortgage loan term. While this is now changing, lenders are still unwilling to finance most manufactured housing on leased land with anything but costly personal property installment loans. In addition, they are reluctant to finance purchase of an existing manufactured home, especially if it has been moved from its original location.

These constraints make credit crunches—largely a thing of the past for buyers of other types of housing—common in the manufactured housing market. They also reinforce the vulnerability of households living in manufactured homes. Some states address the vulnerability issue by offering tenants of leased-land communities first-refusal rights if the land is sold. Tenants in these states have the right to create a collective bid for the estate within a set period of time. If their bid is reasonable, they then have the option of purchasing the estate as a cooperative. In at least one state (Washington), though, the supreme court struck down the state's right-of-first-refusal law, asserting that it interferes with an owner's right to sell.

The Commission recommends that:

- Congress (a) affirm that Fannie Mae and Freddie Mac can purchase manufactured home loans classified as personal property, (b) encourage support of a secondary market in such loans if they are determined to be sound, and (c) establish performance goals for manufactured home loan purchases.
- FHA's Title I and II programs be promoted and loan limits be increased.
- Ginnie Mae approve more lenders as issuers/servicers, or instruct current issuers to make and service loans for manufactured homes.

The Federal Home Loan Banks also play an important role in achieving these housing goals. Although they hold only 2 percent of outstanding mortgage debt,[18] the FHLBs have about $450 billion in outstanding advances to their member banks and thrifts—almost all of which are collateralized by whole mortgages.

In light of the demonstrated value of the GSEs, as well as their potential to help their partners expand homeownership opportunities among immigrants, minorities, and low-income households, the Commission:

- Affirms the ongoing importance of the GSEs to (a) manage the credit and interest-rate risk inherent in mortgage lending, (b) assure the stability and liquidity of the mortgage finance system, and (c) expand homeownership and rental housing opportunities.
- Supports the current regulatory system for Fannie Mae and Freddie Mac, and cautions against modifications that would compromise the integrity of the secondary markets.
- Recommends that Congress and HUD support full, safe, and sound GSE activity in subprime, manufactured housing, home improvement, small multifamily, and development and construction lending. One specific impediment to the full participation of the FHLBs in such new initiatives that should be removed is the restriction on creating subsidiary or affiliated corporations, either on an individual or joint basis. This limitation has hampered the flexibility and efficiency of the FHLBs, and it does not apply to the other GSEs.

15. Early results from the Moving to Opportunity program, a strong randomized experimental design, are mixed. In Boston, early results suggest little impact on employment. See Lawrence F. Katz, Jeffrey R. Kling, and Jeffrey B. Liebman, "Moving to Opportunity in Boston: Early Results on a Randomized Mobility Experiment," *Quarterly Journal of Economics* 116:2 (2001). In Chicago, however, moving to a better neighborhood is, so far, also correlated with positive employment outcomes. Emily Rosenbaum and Laura E. Harris, "Residential Mobility and Opportunities: Early Impacts of the Moving to Opportunity Demonstration Program in Chicago," *Housing Policy Debate* 12:2 (2001): 312-346.

16. Anthony Downs, *Neighborhoods and Urban Development* (Washington, D.C.: The Brookings Institution, 1981). William G. Grigsby and Louis Rosenburg, *Urban Housing Policy* (New York: Center for Urban Policy Research, Rutgers University, 1975). James R. Cohen, "Abandoned Housing: Exploring Lessons from Baltimore," *Housing Policy Debate* 12:3 (2001): 415-448.

17. It remains unclear, however, whether it is flagging demand for the housing in such neighborhoods, independent of the influence of a few vacant properties, that causes both the initial few abandoned properties and the growing many. What is clearer is that demolition is more common in areas with greater concentrations of poverty and concentrations of housing affordable to the poor. This is the finding of a study by Tsuriel Somerville and Cynthia Holmes. Note that the model of filtering and demolition used does not contain a control for rental vacancy rates or proportion of abandoned properties in the zones analyzed. Therefore, concentration of poverty and affordable units may be proxies for other housing market conditions. See C. Tsuriel Somerville and Cynthia Holmes, "Dynamics of the Affordable Housing Stock: Microdata Analysis of Filtering," *Journal of Housing Research* 12:1 (2001): 115-140.

18. U.S. General Accounting Office, *Urban Development Action Grants: An Analysis of Selection Criteria and Program Results* (Washington, D.C., 1989). Ingrid Gould Ellen, Michael Schill, Scott Sussin, and Amy Ellen Schwartz, "Do Homeownership Programs Increase Property Values in Low-Income Neighborhoods?" *Low-Income Homeownership: Examining the Unexamined Goal* (Washington, D.C.: Brookings Press, expected 2002).

19. Anthony Downs, *New Visions for Metropolitan America* (Washington, D.C.: The Brookings Institution, 1994).

20. Frank E. Nothaft, *Trends in Homeownership and Home Equity: Report to the Consumer Federation of America's National Forum to Promote Lower-Income Household Savings* (Washington, D.C.: November 2000).

21. In 2001, the average homeowner lowered their interest rate by 115 basis points. This led to a $10 billion savings in 2001 (based on an average loan size of $132,000) and a monthly average savings of approximately $100. Freddie Mac, *Homeowners Dramatically Lowered Their Mortgage Rates in 2001 as Housing Continued to Shore Up Economy* (Washington, D.C.: Press Release, February 20, 2002).

22. Leland C. Brendsel, Chairman and CEO, Freddie Mac, *Speech at the Regional Conference of MBAs, General Session* (New Jersey: March 20, 2002).

23. Alan Greenspan, *Mortgage Markets and Economic Activity: Remarks Before a Conference of Mortgage Markets and Economic Activity sponsored by America's Community Bankers* (Washington, D.C.: November 2, 1999).

24. Equivalent payments by homeowners are called "imputed rent." Imputed rent is best thought of as the equivalent rent payment an owner would have to make if they rented a unit of comparable quality and in a comparable home to the one they own.

25. Calculations based on the National Association of Home Builders (NAHB), *The Local Impact of Home Building in Average City, USA* (Washington, D.C.: February 2002). National aggregates calculated by the Millennial Housing Commission using 2001 Housing Start data from the U.S. Bureau of the Census.

26. NAHB estimates local effects of homebuilding by netting out impacts likely to accrue outside the local economy. New multifamily housing produced slightly fewer jobs and wages. Every 100 new multifamily apartments generates about 112 full-time equivalent local jobs, $5.3 million in local income, and $1.97 million in federal, state, and local tax revenues and fees in the first year alone.

15. U.S. Department of Commerce and the U.S. Department of Housing and Urban Development, *1999 American Housing Survey* (Washington, D.C., October 2000).

16. Ann B. Schnare, *Impact of Recent Trends in Multifamily Housing Finance on Older Urban Areas* (Cambridge, MA: Joint Center for Housing Studies, Harvard University, June 2001).

17. These fees can be very high. In the San Francisco Bay area, for example, development impact fees are as high as $65,000 per new owner-occupied unit and over $40,000 per new rental unit. Wendell Cox, *Smart Growth and Housing Affordability* (Washington, D.C.: Prepared for the Millennial Housing Commission, March 2002).

18. The following findings emerge from the literature:

- Exclusionary zoning artificially restricts the supply of land and leads to higher housing prices. See William A. Fischel, *Do Growth Controls Matter? A Review of Empirical Evidence on the Effectiveness and Efficiency of Local Government Land Use Regulation* (Cambridge, MA: Lincoln Institute for Land Policy, 1990). Bruce W. Hamilton, "Zoning and the Exercise of Monopoly Power," *Journal of Urban Economics 5* (1978): 116-130. Louis A. Rose, "Urban Land Supply: Natural and Contrived Restrictions," *Journal of Urban Economics 25* (1989): 325-345. James A. Thorson, "An Examination of the Monopoly Zoning Hypothesis," *Land Economics 72:1* (1996): 43-55. Henry Pollakowski and Susan M. Wachter, "The Effects of Land-Use Constraints on Housing Prices," *Land Economics 66:3* (1990): 315-324. Susan M. Wachter and Man Cho, "Interjurisdictional Price Effects of Land Use Controls," *Journal of Urban & Contemporary Law 40* (1991): 49-63. Richard K. Green, "Land Use Regulation and the Price of Housing in a Suburban Wisconsin County." *Journal of Housing Economics 8* (1999): 144-159.

- Exactions and impact fees drive up housing costs directly for new construction, but also indirectly for existing housing. See Larry D. Singell and Jane H. Lillydahl, "An Empirical Examination of the Effect of Impact Fees on the Housing Market," *Land Economics 66:1* (1990): 82-91. Marla Dresch and Steven M. Sheffrin, *Who Pays for Development Fees and Exactions?* (San Francisco: Public Policy Institute of California, June 1997). Brett M. Baden and Don L. Coursey, *An Examination of the Effect of Impact Fees on Chicago's Suburbs* (Chicago: Irving B. Harris Graduate School of Public Policy Studies, University of Chicago, 2001). See also Mark Skidmore and Michael Peddle, "Do Development Impact Fees Reduce the Rate of Residential Development?" *Growth and Change 29* (Fall 1998): 383-400.

- Growth controls lift prices and rents. See Lawrence Katz and Kenneth Rosen, "The Interjurisdictional Effects of Growth Controls on Housing Prices," *Journal of Law and Economics 30* (1987): 149-160. Ned Levine, "The Effects of Local Growth Controls on Regional Housing Production and Population Redistribution in California," *Urban Studies 36* (1999): 2047-2068. Wendell Cox and Ronald D. Utt, "Smart Growth, Housing Costs and Homeownership," *The Heritage Foundation Backgrounder 1426* (April 6, 2001). Samuel R. Staley and Gerard C. S. Mildner. "Urban-Growth Boundaries and Housing Affordability: Lessons From Portland," *Reason Public Policy Institute, Policy Brief 11* (1999). G. Donald Jud and Daniel T. Winkler, "The Dynamics of Metropolitan Housing Prices," *Journal of Real Estate Research 23:1/2* (2002): 29-45. A recent study using an index of restrictive regulations concluded that rents are 17 percent higher, house values 51 percent higher, and homeownership rates 10 percentage points lower, all else equal, in heavily regulated metropolitan areas. See Richard K. Green and Stephen Malpezzi, *A Primer on US Housing Markets and Housing Policy* (Madison: Center for Urban Land and Economics Research, University of Wisconsin, Working Paper Series, October 4, 2000). Note that this paper's index measure captures qualitative assessments of zoning and subdivision approval times, rezoning times, acreage of land zoned for single-family and multifamily housing in relationship to demand for them, percent of zoning changes approved, and adequacy of roads and sewers. Another paper concluded that permit approval delays and growth control restrictions sharply reduce construction levels. See Christopher J. Mayer and C. Tsuriel Somerville, "Land Use Regulation and New Construction." *Regional Science & Urban Economics 30* (2000): 639-662.

8. *The Final Report of the National Commission on Severely Distressed Public Housing, A Report to the Congress and the Secretary of HUD* (Washington, D.C.: August 1992).

9. Meryl Finkel et al., *Capital Needs of the Public Housing Stock in 1998: Formula Capital Study* (Washington, D.C.: Prepared for the U.S. Department of Housing and Urban Development, January 30, 2000).

10. Funded by annual appropriations.

11. For PHAs with individual scattered-site homes in their inventory, a "property" is probably a group of such homes located near one another, rather than a "project" as defined by HUD.

12. An instrument similar to that used in the Mark-to-Market process could be employed for these assessments, which would also benefit from the significant planning already conducted by many PHAs.

13. As units become vacant.

14. This approach will not work in locations where lack of affordable private rental housing makes vouchers unusable. It is particularly unlikely to work for small rural PHAs.

15. For information on the characteristics of high-poverty neighborhoods, see Sandra J. Newman and Ann B. Schnare, "'...And a Suitable Living Environment': The Failure of Housing Programs to Deliver on Neighborhood Quality," *Housing Policy Debate* 8:4 (1997): 703-742. Paul Jargowsky, *Poverty and Place: Ghettos, Barrios, and the American City* (New York: Russell Sage Foundation, 1997).

16. For more details on this proposal see James G. Stockard, Gregory A. Byrne, et al., *Public Housing Operating Cost Study* (Cambridge, MA: Harvard University, Graduate School of Design, 2001).

17. That is, properties that, once investments are complete, would have market rents capable of supporting the debt service needed to bring them to adequate condition.

18. U.S. Department of Housing and Urban Development, *Resident Characteristics Report for Public Housing* (October 2000).

19. FHA Comptroller's Report to the Commissioner, *FHA Portfolio Analysis: Data as of September 2001* (Washington, D.C., October 2001). Office of the President of the United States, *Budget of the U.S. Government, FY 2003, Appendix* (Washington, D.C.: January 2002).

20. Passed in 1945, the GCCA is the legislation under which wholly owned government corporations are chartered. These include a large number of entities that support themselves through their own revenues.

21. These include equity pay-in rules that make FHA insurance difficult to use with Low Income Housing Tax Credits, a developer's profit calculation (called BSPRA), a cost-certification process that has limited relevance in today's market, and overly complex and costly rules for oversight of wage rate requirements.

22. A properly designed risk-sharing program would rely upon the strengths of the respective partners and have controls to assure partners selected are well capitalized and able to honor risk-sharing commitments. The target market for any program would need to be well understood, including how it related to FHA's current programs and those markets that are already well served by the private sector. The risk-sharing agreement would also need to properly align incentives so that the partner would be motivated to protect FHA against inappropriate losses. See Sarah Rosen Wartell, *Single-Family Risk-Sharing: An Evaluation of its Potential as a Tool for FHA* (Washington, D.C.: Prepared for the Millennial Housing Commission, May 2002).

23. In particular, some believe that there is an important expanded role for FHA to play in the growing subprime mortgage market, but few believe that FHA today has the risk management and delivery systems in place to insure those higher risks prudently. On the other hand, there are potential partners who have the technology, skills, and systems to manage risk, but not the capital or risk tolerance for the subprime market. Risk-sharing with these actors would allow FHA to rationalize underwriting, promote transparency, reduce predatory practices, and enhance price competition in the subprime market.

37. Catalog of Federal Domestic Assistance (http://www.cfda.gov/). Program Number 14.239.

38. National Council of State Housing Agencies, *Ten Year Rule Impact on MRB Mortgage Lending, 2001-2005* (2001).

Supporting Recommendations

(pages 71 to 83)

1. John D. Hawke Jr., "Banking in Indian Country: Challenges and Opportunities," *Community Developments*, Comptroller of the Currency, Fall 2001.

2. Coalition for Indian Housing and Development, June 29, 2001, response to Millennial Housing Commission solicitation letter.

3. *One Stop Mortgage Center Initiative in Indian Country: A Report to the President* (Washington, D.C.: U.S. Department of Housing and Urban Development, U.S. Department of the Treasury, October 2000).

4. *The Report of the Native American Lending Study*, CDFI Fund, U.S. Department of the Treasury.

5. Mr. Campbell, *Providing for Business Development and Trade Promotion for Native Americans, and for Other Purposes* (Washington, D.C.: Report 106-139, 106th Congress, September 1999).

6. *Native American Housing News*, Special Convention Issue, 2001.

7. Hawaiian Community Assets, letter to the Millennial Housing Commission, October 16, 2001.

8. U.S. Bureau of the Census, *Reason Modestly Priced Home Cannot be Afforded* (Washington, D.C.: 1995).

9. Funds from the $200 million American Dream Downpayment Fund, part of the President's budget for fiscal year 2003, could be used as matching grants for IHDAs.

10. *Merriam-Webster's Collegiate Dictionary*, online version.

11. State-issued housing bonds issued prior to the 1986 Tax Reform Act are exempt from AMT, making this comparison possible. "Comparison of Interest Rates on Housing Bond Issues Sold during Week of January 28, 2002," *The Bond Buyer* (February 2002).

12. "Quarterly Financing Survey, 3rd Quarter 2001: Summary Findings," *National Association of Home Builders* (March 2002).

13. Abdighani Hirad and Peter Zorn, *A Little Knowledge is a Good Thing: Empirical Evidence of the Effectiveness of Pre-Purchase Homeownership Counseling* (Washington, D.C.: Freddie Mac, May 21, 2001).

14. Hugh Mahoney and Peter Zorn, "Promise of Automated Underwriting," *Secondary Mortgage Markets* 13:3 (November 1996).

15. Calculations by the Millennial Housing Commission based on placement data from the U.S. Census–Manufactured Homes Survey, March 2002, and the U.S. Census Survey of New Residential Construction (one-unit structures), March 2002.

16. Michael Collins, David Crowe, and Michael Carliner, "Examining Supply-Side Constraints to Low-Income Homeownership," *Low-Income Homeownership: Examining the Unexamined Goal* (Washington D.C.: Brookings Press, expected 2002).

17. National Association of Home Builders–Research Center, *Factory and Site-Built Housing: A Comparison for the 21st Century* (Washington, D.C.: NAHB, October 1998).

18. Marsha Courchane, David Nickerson, and Frank Nothaft, *Evolution of the Housing Finance System in America* (Washington, D.C.: Freddie Mac working paper, prepared for the Millennial Housing Commission, May 2002).

Table 1 | *Household and Housing Stock Characteristics by Income, 1999 (Thousands)*

	Owners					Renters					
	ELI [1]	VLI	LI	MI	HI	ELI [1]	VLI	LI	MI	HI	Total
Households											
Total Households	6,410	7,138	10,680	14,284	30,283	8,513	6,243	7,270	6,681	5,300	102,802
Not Burdened (0-30%)[2]	1,854	4,259	7,571	11,888	28,701	2,134	2,172	5,034	6,092	5,174	74,879
Moderately Burdened (30-50%)	1,372	1,728	2,328	1,931	1,344	1,580	2,950	1,984	496	110	15,823
Severely Burdened (>50%)	3,175	1,151	783	465	239	4,798	1,121	252	93	15	12,092
Working Status of Households											
Earning at Least FTE Minimum Wage	393	2,647	7,024	11,478	28,136	1,110	4,452	6,603	6,056	5,108	73,007
Number with Severe Cost Burdens	167	582	564	383	217	482	679	197	82	8	3,361
Earning Between Half and FTE Minimum Wage	598	515	495	180	204	1,631	606	131	22	19	4,401
Number with Severe Cost Burdens	268	96	28	5	-	984	130	2	-	2	1,515
Earning Less than Half FTE Minimum Wage	703	355	349	210	156	1,710	146	57	15	17	3,718
Number with Severe Cost Burdens	514	59	25	16	2	1,311	43	5	-	-	1,975
Elderly, Not Working	3,188	3,086	2,396	1,678	1,306	1,721	749	377	197	100	14,798
Number with Severe Cost Burdens	1,392	290	118	32	7	898	181	42	12	5	2,977
Non-elderly, Not Working	1,528	537	416	738	481	2,340	291	102	389	55	6,877
Number with Severe Cost Burdens	843	124	46	29	13	1,124	88	7	-	-	2,274
Affordable Housing Stock											
Units Affordable at 30% of income	6,606	11,669	23,475	17,053	11,445	6,681	12,092	14,222	2,950	1,073	107,266
Affordable and Available	1,724	3,778	7,322	6,324	11,445	3,570	6,631	7,231	1,645	1,073	50,743
Gap between Available Units and Households	(4,686)	(3,360)	(3,358)	(7,960)	(18,838)	(4,943)	388	(39)	(5,036)	4,227	(52,059)
Adequate	5,586	10,602	22,280	16,440	10,962	5,288	9,598	11,845	2,483	840	95,924
Moderately Inadequate	511	548	539	289	169	609	1,116	867	121	56	4,825
Severely Inadequate	168	171	302	161	67	330	397	381	61	15	2,053
Vacant: No Information	341	347	354	163	247	454	981	1,129	285	162	4,463

Notes:

1. ELI (extremely low income) defined as having incomes at or below 30% of AMI; VLI (very low income) defined as having incomes 30.1-50% of AMI; LI (low income) defined as having incomes 50.1-80% of AMI; MI (moderate income) defined as having incomes 80.1-120% of AMI; HI (high income) defined as having incomes over 120% of AMI.
2. Households in the "not burdened" group include those reporting zero or negative income. Depending on their reported housing costs, the households were included in ELI or MI.

Source: HUD tabulations of the 1999 American Housing Survey prepared for the Millennial Housing Commission.

Table 3 | *Stock of Federally Assisted Units by Funding Source, 1999*

	Thousands of Units
Inactive: Publicly Owned, Project-Based	
Public Housing	1,274
Inactive: Privately Owned, Project-Based	
Section 8 New Construction / Substantial Rehabilitation	644
Section 202 Elderly Housing Direct Loan	207
Section 8 Property Disposition	60
Section 8 Loan Management Set-Aside	409
Rent Supplement	21
Section 236	60
Section 221(d)(3) Below Market Interest Rate	71
Active: Tenant-Based	
Section 8 Certificates and Vouchers	1,581
Active: Privately Owned, Project-Based	
Section 202 Supportive Housing for the Elderly	65
Section 811 Supportive Housing for Persons with Disabilities	18
Section 515 Rural Housing Rental Assistance	410
Total Rental Assistance	**4,820**
Total Owner Assistance	**591**
Total Direct Assistance	**5,411**

Note: Numbers are adjusted for overlap based on HUD's *A Picture of Subsidized Households, 1998*, RHS data, and GAO's *Tax Credits: Opportunities to Improve Oversight of the Low-Income Housing Program*, GAO/GGD/RCED-97-55.

Sources: GAO, *Federal Housing Assistance: Comparing the Characteristics and Costs of Housing Programs*, GAO-02-76; HUD Budget Office; Rural Housing Service, Deputy Administrator for Single-Family Housing; and U.S. House of Representatives, *2000 Green Book*.

Median Housing Cost as Percent of Income	Housing Costs					
	Under 30% of Income		30-50% of Income		Over 50% of Income	
	Number	Percent	Number	Percent	Number	Percent
58	2.1	25	1.6	18	4.8	56
35	2.2	35	3.0	48	1.1	18
25	5.0	69	2.0	27	0.3	3
19	6.1	92	0.5	8	0.1	1
12	5.2	98	0.1	2	0.0	0
25	20.6	61	7.2	21	6.3	18
50	1.9	29	1.4	21	3.2	50
25	4.3	60	1.7	24	1.2	16
21	7.6	71	2.3	22	0.8	7
17	11.9	83	1.9	14	0.5	3
13	28.7	95	1.3	4	0.2	1
17	54.4	79	8.6	13	5.9	8
54	4.0	27	3.0	20	8.0	54
31	6.5	48	4.7	35	2.3	17
23	12.6	70	4.3	24	1.1	6
18	18.0	86	2.4	12	0.6	3
13	33.9	95	1.4	4	0.2	1
19	75.0	73	15.8	15	12.2	12

Table 6 | ***Households Receiving Direct Housing Assistance Administered by HUD, 1977-2000***

	Assisted Renters					
	Existing Housing					
	Tenant-Based[1]	Project-Based[2]	New Construction[3]	Total Assisted Renters[4]	Total Assisted Homeowners[5]	Total Assisted Households
1977	162	105	1,799	2,067	331	2,398
1978	297	126	1,928	2,350	293	2,643
1979	427	175	1,978	2,580	262	2,842
1980	521	185	2,090	2,797	235	3,032
1981	599	221	2,228	3,212	219	3,431
1982	651	194	2,373	3,379	241	3,620
1983	691	265	2,485	3,615	242	3,857
1984	728	357	2,589	3,851	230	4,081
1985	749	431	2,657	4,015	210	4,225
1986	797	456	2,686	4,135	200	4,335
1987	893	473	2,721	4,279	182	4,461
1988	956	490	2,736	4,371	159	4,530
1989	1,025	509	2,748	4,485	148	4,633
1990	1,090	527	2,755	4,569	141	4,710
1991	1,137	540	2,778	4,656	130	4,786
1992	1,166	554	2,786	4,705	125	4,830
1993	1,326	574	2,762	4,861	98	4,959
1994	1,392	593	2,764	4,939	95	5,034
1995	1,474	607	2,778	5,049	80	5,129
1996	1,413	608	2,817	5,028	76	5,104
1997	1,465	586	2,822	5,063	68	5,131
1998	1,481	564	2,786	5,021	60	5,081
1999	1,613	542	2,757	5,101	53	5,154
2000	1,621	522	2,728	5,061	43	5,104

Notes:

1. Includes units assisted with Section 8 certificates and vouchers.
2. Includes units assisted through the Section 8 Loan Management Set Aside, PD, Conversion (from rent supplement and Section 236 Rental Assistance Program), and Moderate Rehabilitation Programs.
3. Includes units assisted through the Section 8 New Construction and Substantial Rehabilitation Program, Section 236, Rent Supplement, and Public Housing Programs (including Indian units constructed under Public Housing but now assisted through the other programs).
4. The total number of assisted renters has been adjusted since 1980 to avoid double-counting of households receiving more than one type of subsidy. The total number therefore is lower than the sum of the components.
5. Includes units assisted through various Section 235 programs.

Source: *2000 Green Book: Background Material and Data on Programs within the Jurisdiction of the Committee of Ways and Means*, U.S. House of Representatives, October 6, 2000.

Table 8 | ***Key Federal Housing Budget Trends (Billions of Constant 2002 Dollars)***

Federal Spending for Housing	1977-1981	1982-1986	1987-1991	1992-1996	1997-2001	2002-2007
Assisted Housing Outlays	$4.9	$13.5	$14.9	$23.7	$28.6	$33.8
Assisted Housing Budget Authority	$28.1	$15.3	$12.0	$18.8	$18.6	$31.4
Tax Expenditures	$44.8	$63.7	$90.9	$107.5	$117.9	$120.2
All HUD Outlays	$10.1	$18.1	$19.4	$26.0	$31.1	$34.0
All HUD BA	$78.8	$33.3	$24.2	$27.9	$25.4	$35.2

Federal Tax Expenditures for Housing	1977-1981	1982-1986	1987-1991	1992-1996	1997-2001	2002-2007
Mortgage Interest Deductions	$25.2	$39.4	$49.6	$55.4	$60.0	$66.3
Property Tax Deductions	$14.5	$13.9	$13.9	$16.5	$21.3	$19.2
Capital Gains	$2.9	$3.9	$15.7	$21.8	$22.4	$20.1
Other Homeowner	$0.1	$0.9	$0.0	$0.0	$0.0	$0.0
Homeowner Subtotal	$42.7	$58.1	$79.3	$93.7	$103.6	$105.5
Investor Deductions	$2.1	$5.6	$11.6	$13.8	$14.3	$14.7
Total	$44.8	$63.7	$90.9	$107.5	$117.9	$120.2

Source: National Low Income Housing Coalition, *Changing Priorities: The Federal Budget and Housing Assistance, 1996-2006,* 2001.

Table 10 | ***Terms on Conventional Single-Family Mortgages, 1980-2001 (Annual National Averages, All Homes)***

Year	Effective Interest Rate (%)	Term to Maturity (Years)	Mortgage Loan Amount (1000s of 2001 Dollars)	Purchase Price (1000s of 2001 Dollars)	Loan-to-Price Ratio	Percent of Loans With: Loan-to-Price Ratio Above .9	Percent of Loans With: Adjustable Rates
1980	12.8	27.2	111.1	157.8	72.9	10	n/a
1981	14.9	26.4	104.6	148.7	73.1	15	n/a
1982	15.3	25.6	100.9	143.9	72.9	21	41
1983	12.7	26.0	106.5	147.8	74.5	21	40
1984	12.5	26.8	109.9	147.6	77.0	27	62
1985	11.6	25.9	115.5	158.2	75.8	21	51
1986	10.2	25.6	128.1	178.7	74.1	11	30
1987	9.3	26.8	138.9	189.9	75.2	8	43
1988	9.3	27.7	145.8	197.0	76.0	8	58
1989	10.1	27.7	149.3	204.0	74.8	7	38
1990	10.1	27.0	140.9	193.2	74.7	8	28
1991	9.3	26.5	138.2	190.8	74.4	9	23
1992	8.1	25.4	137.2	184.8	76.6	14	20
1993	7.1	25.5	131.1	175.4	77.2	17	20
1994	7.5	27.1	131.3	169.7	79.9	25	39
1995	7.9	27.4	128.3	165.9	79.9	27	32
1996	7.7	26.9	134.0	175.1	79.0	25	27
1997	7.7	27.5	139.7	181.5	79.4	25	22
1998	7.1	27.8	143.2	188.4	78.9	25	12
1999	7.3	28.2	148.1	195.8	78.5	23	21
2000	8.0	28.7	152.5	204.6	77.8	22	24
2001	7.0	27.6	155.7	215.5	76.2	21	12

Source: Federal Housing Finance Board, Monthly Interest Rate Survey.

done to ensure a more conservative estimate of the extent of housing affordability problems since there is no way to discern which of these households may be cost-burdened. Households who reported paying no cash rent were also considered to have no housing cost burden.

Affordable Units by Income Range

Each unit included in the American Housing Survey was placed into an affordability category by comparing its gross rent or estimated ownership cost (described below) to the household income cutoffs noted above. A unit was considered affordable to an income group if the gross rent or estimated ownership cost fell between 30 percent of the monthly income that demarcated the top and bottom of the income group. To approximate the actual number of affordable units, the Commission excluded those identified as "seasonal" or "usual residence elsewhere" (URE), which are typically second homes and unavailable to households seeking affordable housing.

To sort units by income group, the Millennial Housing Commission attempted to include all housing costs in the measurement. To this end, utility costs for vacant units had to be imputed or allocated. These allocations are based on four factors: monthly housing costs (rent or mortgage payment), structure type (single- or multifamily), region of the country (census region), and tenure (owner or renter). Reported monthly principal and interest payments for owner-occupied units varied widely and therefore did not correlate well with property values. To standardize owner-occupied housing costs, the MHC assumed a 30-year mortgage with a 7-percent interest rate as well as a 10-percent downpayment, plus the cost of utilities, taxes, and insurance.

The final calculation to ensure that housing units were grouped appropriately was to adjust the threshold for affordable rents by bedroom size. The following adjustments were made to reflect the size of the households that would occupy the unit:

0 bedrooms:	AMI * 0.70	4 bedrooms:	AMI * 1.16
1 bedroom:	AMI * 0.75	5 bedrooms:	AMI * 1.28
2 bedrooms:	AMI * 0.90	6 bedrooms:	AMI * 1.40
3 bedrooms:	AMI * 1.04	7+ bedrooms:	AMI * (1.40 + 0.12 per bedroom over 6)

Earnings Classifications

The Millennial Housing Commission was also interested in determining the working status of households. To this end, households were first sorted by total household income. Wage and salary earnings within each income group were then calculated, and households were again sorted into four groups: those with zero wage earnings, less than half the full-time equivalent of minimum wage, half- to full-time minimum wage, or greater than minimum wage. Households were then classified by cost burden, based on housing costs relative to total household income.

Household groups were also sorted by age to identify which were elderly (65 or older) and non-elderly (younger than 65). To examine the cost burdens and characteristics of some working households, a second set of tabulations was run using salary cutoffs based on the average incomes of several professions.

Rental Assistance

Section 202
Supportive Housing for the Elderly

Enactment	Housing Act of 1959
Program Description	Direct federal grants and project-based Section 8 subsidies to nonprofit sponsors to finance rental or cooperative housing for the elderly.
Tenant Eligibility	Only households with heads 62 years or older and with very low incomes.
Rent Structure	Tenants pay the greater of 10% of monthly income or 30% of adjusted monthly income.
Number of Existing Units	65,000
FY 2001 Budget Authority	$779,000,000
FY 2001 Outlays	See Section 811 below.
Current Status	Approximately 6,500 units are funded annually in recent years.

Section 811
Supportive Housing for Persons with Disabilities

Enactment	Cranston-Gonzalez Affordable Housing Act of 1990
Program Description	Direct federal grants and project-based Section 8 subsidies to nonprofit sponsors to finance rental or cooperative housing for the disabled.
Tenant Eligibility	Available only for very low-income people with disabilities.
Rent Structure	Tenants pay the greater of 10% of monthly income or 30% of adjusted monthly income.
Number of Existing Units	18,000
FY 2001 Budget Authority	$217,000,000
FY 2001 Outlays	Section 202 and 811 had $774,000,000 in combined outlays.
Current Status	Approximately 1,650 units have been funded annually in recent years.

Section 221(d)(3)
Section 221(d)(4)
Multifamily Rental Housing for Moderate-Income Families

Enactment	National Housing Act of 1961
Program Description	HUD insures mortgages made by private lenders to help finance construction or substantial rehabilitation of multifamily rental or cooperative housing for moderate-income or displaced families. The principal difference between the two programs is that HUD may insure up to 100% of total project cost under Section 221(d)(3) for nonprofit and cooperative mortgagors, but only up to 90% under Section 221(d)(4), regardless of the type of mortgagor.
Applicant Eligibility	Section 221(d)(3) and 221(d)(4) mortgages may be obtained by public agencies; nonprofit, limited dividend, or cooperative organizations; private builders; or investors who sell completed projects to such organizations. Section 221(d)(4) mortgages may also be obtained by profit-motivated sponsors.
Tenant Eligibility	Tenant occupancy is not restricted by income limits. Projects may be designed specifically for the elderly or handicapped.
FY 2001 Program Level	$2,353,706,686 in mortgages insured

Section 8 New Construction and Substantial Rehabilitation	Enactment	Housing and Community Development Act of 1974
	Program Description	Subsidy to fill gap between tenant rent and contract rent for the unit. Subsidy commitment to owner for 20-40 years provides incentive for construction and for owner to reserve units for low-income tenants. Many projects were built with Section 202 direct loans for elderly housing.
	Tenant Eligibility	Income below 80% of the area median, adjusted for family size. Forty percent of new admissions each year must have incomes below 30% of area median.
	Rent Structure	Tenants pay the greater of 10% of monthly income or 30% of monthly adjusted income in rent.
	Number of Existing Units	850,766 (including 207,131 built under the original Section 202 direct loan program)
	Current Status	No new commitments since 1983.

Section 8 Moderate Rehabilitation	Enactment	1978
	Program Description	Rental subsidy administered by the housing authority and tied to rehabilitated units. Subsidy commitment to owner is 15 years.
	Tenant Eligibility	Income lower than 50% of the area family median, adjusted for family size.
	Rent Structure	Rents are limited to 125% of the local fair market rent (FMR) for comparable Section 8 Existing units.
	Current Status	No new commitments since 1991.

Section 8 Certificate and Voucher (Existing Housing) Program	Enactment	Housing and Community Development Act of 1974 (certificates) and 1987 (vouchers). In 1998, the Quality Housing and Work Responsibility Act (QHWRA) merged the two programs into the housing choice voucher program.
	Program Description	Vouchers that pay property owner the difference between 30% of the tenant's income and the lower of the unit rent or a payment standard. Any unit meeting program housing quality standards with a reasonable (i.e., market comparable) rent that leases for no more than the FMR is eligible. Recipients are chosen by local PHAs from Section 8 waiting lists. Recipients have the freedom and responsibility to find housing that meets program quality and rent standards. If recipients' existing housing units meet standards and are available at a reasonable rent, they do not need to move.
	Tenant Eligibility	Income must not exceed 50% of the area median adjusted for family size or, on an exception basis, 80% of the area median. At least 75% of families admitted to the voucher program must have extremely low incomes (not exceeding 30% of area median).
	Rent Structure	Tenants pay the greater of 10% of monthly income or 30% of adjusted monthly income in rent. Tenants may choose to rent units for more or less than the payment standard. When initially leasing a unit where the gross rent exceeds the payment standard, a tenant may not pay more than 40% of adjusted monthly income.
	Number of Existing Units	1.8 million
	FY 2001 Budget Authority	$11,970,000,000
	FY 2001 Outlays	$16,720,000,000
	Current Status	In recent years, an average of 38,000 vouchers have been added to the budget annually. In 2001, the voucher utilization rate (defined as the percentage of available vouchers under lease or the percentage of annual budget authority spent) was 93%. In 2002, the utilization rate is estimated at 95%. In comparison, the national voucher

	FY 2001 Program Level	As of May 2001, $53,900,000 in payments from the FHA fund had been made since the Office of Multifamily Housing Assistance Restructuring (OMHAR) came into existence. The Mark-to-Market program is expected to result in Section 8 program savings of $218 million in FY 2002.
	Number of Existing Units	About half of the HUD-insured Section 8 portfolio is estimated to have above-market rents and eventually enter the Mark-to-Market program. OMHAR estimates that about 62% of those would receive full mortgage restructuring and the remaining 38% would receive rent restructuring only.
	Current Status	As of June 15, 2001, OMHAR had contracts with 33 administrative entities and the number of properties in the program was 1,558. OMHAR had completed restructurings for 138 of the properties requiring full mortgage restructurings and 500 of those requiring only rent reductions. OMHAR estimates that the restructurings will result in about $563,000,000 in federal savings over a 20-year period. In January 2002, President Bush signed legislation extending the program for another five years.
Section 515 Rural Rent Housing Direct Loans	Enactment	Housing Act of 1949
	Program Description	Direct loans made to developers at 1% interest rate through the Rural Housing Service (RHS) of the U.S. Department of Agriculture. Payments are made directly from the federal government to the developer.
	Tenant Eligibility	Tenants must have incomes at or below 80% of area median. Households with incomes below 50% of median may receive additional assistance through the HUD Section 8 program or the FmHA Section 521 program.
	Rent Structure	Tenants may obtain rental assistance through the Section 521 program, which provides funds directly to developers so that tenants pay no more than 30% of adjusted income for rent and utilities. The developer receives enough rent to cover mortgage costs, with any excess going back to the government to offset the reduced interest rate.
	Number of Existing Loans	484,672 (including 45,000 Section 8 units)
	FY 2001 Authorized Level	$114,000,000 (direct loan level supportable by subsidy budget authority)
	FY 2001 Program Level	In FY 2001, $1,212,000,000 new disbursements were made for all RHS direct loan programs, including the Section 515 program.
	Current Status	Through 2000, 523,609 loans had been made through the Section 515 direct loan program.

Homeownership Assistance

Section 235 Low-Income Homeownership Program	Enactment	Housing Act of 1968
	Program Description	Interest rate subsidy to low- and moderate-income homeowners. In its initial form, the interest rate could be reduced as low as 1% to limit mortgage payments to 20% of income. Subsidy is attached to the unit, not the family, and is non-transferable.
	Homebuyer Eligibility	Homebuyers must have incomes at or below 95% of area median.
	Number of Existing Units	31,176
	Current Status	No funding since 1974.

		people (842 jurisdictions), and urban counties with at least 200,000 people (147 counties) automatically qualify for formula-based funds. All other jurisdictions receive their funds through the state.
	Recipient Eligibility	At least 70% of all funds must be used for people with low or moderate incomes. The national average share used for these groups is 90%.
	FY 2001 Budget Authority	$5,112,000,000
	FY 2001 Outlays	$4,939,000,000
	Current Status	The CDBG program receives widespread political support for providing local flexibility in community development. Since its inception, approximately 28% of CDBG funds have gone to housing. In FY 2001, housing's share was 35%.
HOME Investment Partnerships	Enactment	National Affordable Housing Act of 1990
	Program Description	Block grants to localities to expand the supply of affordable housing. Uses include acquisition, rehabilitation, and new construction of rental units; development of homeownership units; direct assistance to homebuyers; and tenant-based rental assistance.
	Applicant Eligibility	States, cities, urban counties, and consortia (of contiguous units of general local governments with a binding agreement) are eligible to receive formula allocations.
	Beneficiary Eligibility	The maximum income for HOME-assisted rental housing units is set at 80% of area median adjusted for family size. However, 90% of families receiving rental assistance from a fiscal year's allocation must have incomes of no more than 60% of area median family income. In projects with five or more HOME units, at least 20% of the units must be affordable to households earning no more than 50% of the area median income. Assisted homeowners and homebuyers must earn less than 80% of the area median income.
	Number of Existing Units	627,000 units created, rehabilitated, or purchased with funds committed; 72,000 families have received tenant-based rental assistance.
	FY 2001 Budget Authority	$1,796,000,000
	FY 2001 Outlays	$1,424,000,000
	Current Status	Funding for the program continues. Households with incomes below 30% of area median occupy 45% of HOME rental housing; 97% of recipients have less than 50% of area median income. Recent annual production has been 55,000-85,000 units annually.
Empowerment Zones and Enterprise Communities	Enactment	Omnibus Budget Reconciliation Act of 1993
	Program Description	Project grants and tax relief to distressed neighborhoods to encourage economic revitalization and job creation, as well as move residents toward self-sufficiency. Recipients of Empowerment Zone designation receive $10 million per year for 10 years as well as access to $2.2 billion in tax-exempt bond authority. Enterprise Communities alternatively receive a smaller grant of $3 million per year.
	Recipient Eligibility	Criteria for urban areas: Areas of pervasive poverty and unemployment and general distress; maximum population of 200,000 or 20 square miles or less in area; a continuous boundary, or consists of not more than six noncontiguous parcels, with the total noncontiguous are a no more than 2,000 acres; located entirely within the jurisdiction of the application group; 90% of census tracts in the zone must have a poverty rate of at least 25% and none may have less than 20%; may not include any part of the CBD unless the

Applicant Eligibility	Entitlement grants are awarded by formula to states and qualifying cities for eligible metropolitan statistical areas (EMSAs) with the largest numbers of cases of AIDS. The most populous city serves as the applicant / grantee for the award. Competitive grants are also awarded to (a) states, local governments, and nonprofit organizations for special projects of national significance, and (b) projects submitted by states and localities in areas that do not qualify for HOPWA formula allocations. Nonprofit organizations can apply for projects of national significance and may also serve as a project sponsor for other types of grants.
Beneficiary Eligibility	Beneficiaries are low-income persons with HIV or AIDS and their families. Regardless of income, persons with AIDS may receive housing information. Persons living near community residences may receive educational information.
Rent Structure	When the grant is used for rental housing, rents cannot exceed 30% of tenant incomes.
Number of Existing Units	HOPWA funds have been used for either operating costs or capital development of approximately 8,000 units.
FY 2001 Budget Authority	$258,000,000
FY 2001 Outlays	$241,000,000
Current Status	In FY 1999, HOPWA provided housing assistance to 51,875 people; 68% of the funds went to housing assistance.

Mortgage Insurance and Loan Guarantees

FHA-Single Family

Enactment	National Housing Act of 1934
Program Description	Mortgage insurance provided through private lenders to enhance the credit of homebuyers and help them qualify for mortgages. The Section 203(b) program is currently the primary FHA single-family mortgage insurance program and provides mortgage insurance without a subsidy.
Eligibility	There are no income limits for this program. Insurance premiums vary based on the applicant's loan-to-value (LTV) ratio.
Loans Outstanding	810,995 at the end of 2000
FY 2001 Authorized Level	$160,000,000,000 (guaranteed loan level supportable by subsidy budget authority)
FY 2001 Program Level	$107,449,000,000 in insurance written
Current Status	Since 1934, FHA and HUD have insured the mortgages on 30 million homes.

FHA-Multifamily

Enactment	National Housing Act of 1934
Program Description	Mortgage insurance provided for credit enhancement of privately developed multifamily properties. The primary programs are the Section 221(d)(4) and Section 221(d)(3) programs for the construction and substantial rehabilitation of multifamily rental or cooperative housing, and the Section 223(f) program for the purchase and refinance of existing multifamily rental properties.
Tenant Eligibility	There are no specific tenant requirements for FHA multifamily loans.
Number of Existing Units	An estimated 1.4 million units are in developments with active insurance contracts.
FY 2001 Authorized Level	$10,685,000,000 (guaranteed loan level supportable by subsidy budget authority)

Private Activity Bonds	Enactment	Private activity bonds were referred to as Industrial Development Bonds before the Tax Reform Act of 1986. (See Tax-Exempt Multifamily Bonds, below.)
	Program Description	Tax-exempt bond issuances from the state that have a public benefit but can be used by private individuals. A per capita allocation is provided to each state, with a "small state minimum" of $225 million. Uses include single-family and multifamily housing, manufacturing facilities, student loans, transportation, and municipal services, among others.
	FY 2002 Authorized Level	$24,216,606,217
	FY 2001 Program Level	$3,750,000,000 (outlay equivalent of tax expenditures)
	Current Status	Per capita allocation was put in place in 1986 and set at $50. This amount was raised in 2001 and will now increase with inflation.
Mortgage Revenue Bonds	Enactment	Single-family bonds were authorized by the Tax Code of 1954 and generally followed Industrial Development Bond rules until enactment of the Mortgage Subsidy Bond Tax Act of 1980. This act created "mortgage subsidy bonds" and restricted their issuance through various requirements, including purchase price limits.
	Program Description	Low interest-rate bonds issued as part of the private activity bond authority are used to provide below-market interest rate mortgages to first-time homebuyers to lower the costs of homeownership.
	Homebuyer Eligibility	First-time homebuyers with up to median income (either state or area). The cost of the home cannot exceed 90% of the area average purchase price. In disadvantaged areas, income and price limits can be higher.
	2000 Program Level	$10,767,892,177 (total 2000 issuance); $1,150,000,000 (outlay equivalent)
	Current Status	Through 2000, 2,177,873 loans had been made through the MRB program. Most loans are used to assist homebuyers with incomes below the program limits.
Tax-Exempt Multifamily Bonds	Enactment	Tax-exempt multifamily bonds were authorized under the Tax Code of 1954 as Industrial Development Bonds. The 1986 Tax Reform Act prohibited issuance of industrial development bonds except for certain purposes, such as creation of rental housing.
	Program Description	Authority for state HFAs to issue bonds (private activity, taxable, nonprofit, or government purpose) for multifamily housing. Bonds for nonprofits are uncapped; issuances for all other groups have limits.
	Project Eligibility	Developers have two ways to meet affordability requirements—20% of the units in the development must be available to tenants with less than 50% of area median income, or 40% of the units must be occupied by tenants with incomes of less than 60% of area median.
	Rent Structure	Rents must be held at a reasonably affordable level "consistent with other federal programs." This is generally interpreted as no more than 30% of the selected income thresholds.
	Number of Existing Units	766,392 as of the end of 2000
	2000 Program Level	$1,668,713,563 (total new issuances); $280,000,000 (outlay equivalent)
	Current Status	This program financed 52,000 units in 2000. Three-quarters of these units were affordable to families with 60% or less of area median income.

Appendix 4 | *Acronyms Used in Report*

ACC	Annual Contributions Contract
AIDS	Acquired Immune Deficiency Syndrome
AMI	area median income
AMT	alternative minimum tax
BMIR	below-market interest rate
CBD	central business district
CBO	Congressional Budget Office
CDBG	Community Development Block Grant
CDC	community development corporation
CDFI	Community Development Financial Institution
CRA	Community Reinvestment Act
DOI	U.S. Department of the Interior
DOL	U.S. Department of Labor
DOT	U.S. Department of Transportation
EITC	earned income tax credit
ELI	extremely low income
EMSA	eligible metropolitan statistical area
EZ/EC	Empowerment Zone / Enterprise Community
FASIT	Financial Asset Securitization Investment Trust
FHA	Federal Housing Administration
FHAP	Fair Housing Assistance Program
FHIP	Fair Housing Initiatives Program
FHLB	Federal Home Loan Bank
FHLMC	Federal Home Loan Mortgage Corporation (Freddie Mac)
FmHA	Farmers Home Administration
FMR	Fair Market Rent
FNMA	Federal National Mortgage Association (Fannie Mae)
FSS	Family Self-Sufficiency program
GAO	General Accounting Office
GCCA	Government Corporation Control Act
GDP	Gross Domestic Product
GI/SRI	General Insurance and Special Risk Insurance fund
GNMA	Government National Mortgage Association (Ginnie Mae)
GSE	government-sponsored enterprise
HAP	Housing Assistance Payment
HDR	*Housing and Development Reporter*
HFA	housing finance agency
HHS	U.S. Department of Health and Human Services
HI	high income
HIV	human immunodeficiency virus
HOME	Home Investment Partnerships Program
HOPWA	Housing Opportunities for Persons with AIDS
HQS	Housing Quality Standards
HUD	U.S. Department of Housing and Urban Development
IBC	International Building Code
IHDA	Individual Homeownership Development Account
IRA	Individual Retirement Account
IRC	Internal Revenue Code
LI	low income
LIHTC	Low Income Housing Tax Credit
LTV	loan to value
MAP	Multifamily Accelerated Processing
MFIP	Minnesota Family Investment Program
MI	moderate income
MRB	Mortgage Revenue Bond
MSA	metropolitan statistical area
MTO	Moving to Opportunity program
NAHASDA	Native American Housing Assistance and Self Determination Act
NCDI	National Community Development Initiative
NOFA	Notice of Funding Availability
OFHEO	Office of Federal Housing Enterprise Oversight
OMB	Office of Management and Budget
OMHAR	Office of Multifamily Housing Assistance Restructuring
PHA	public housing authority or agency
PHAS	Public Housing Assessment System
PHMAP	Public Housing Management Assessment Program
PTI	preservation tax incentive
QAP	Qualified Allocation Plan
QHWRA	Quality Housing and Work Responsibility Act of 1998
RAP	Rental Assistance Payment
REMIC	Real Estate Mortgage Investment Conduit
RESPA	Real Estate Settlement Procedures Act
RHS	Rural Housing Service
TANF	Temporary Assistance to Needy Families
TILA	Truth in Lending Act
VA	Veterans Administration
VLI	very low income
WIA	Workforce Investment Act

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