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S. HRG. 107–1014

AFFORDABLE HOUSING PRESERVATION

HEARING

BEFORE THE

SUBCOMMITTEE ON HOUSING AND TRANSPORTATION

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDRED SEVENTH CONGRESS

SECOND SESSION

ON

PRESERVING THE EXISTING PRIVATELY-OWNED AFFORDABLE HOUSING STOCK CURRENTLY SUPPORTED WITH PUBLIC FUNDS UNDER A VARIETY OF FEDERAL HOUSING INSURANCE, SUBSIDY, AND ASSISTANCE PROGRAMS

OCTOBER 9, 2002

Printed for the use of the Committee on Banking, Housing, and Urban Affairs

U.S. GOVERNMENT PRINTING OFFICE

90–543 PDF WASHINGTON : 2003

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
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AFFORDABLE HOUSING PRESERVATION

WEDNESDAY, OCTOBER 9, 2002

U.S. SENATE,
SUBCOMMITTEE ON HOUSING AND TRANSPORTATION,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Subcommittee met at 2:32 p.m., in room SD–538 of the Dirksen Senate Office Building, Senator Jack Reed (Chairman of the Subcommittee) presiding.

OPENING STATEMENT OF SENATOR JACK REED

Senator REED. Let me call the hearing to order. Good afternoon. I would like to welcome everyone to today's oversight hearing on affordable housing preservation.

We are holding this HUD oversight hearing because there is growing evidence that HUD is neglecting one of its most important responsibilities—its responsibility to preserve and to maintain our Nation's existing affordable housing stock.

Some of our past hearings have highlighted the incredible need for affordable housing in this country. One out of every seven American families spends more than half of their total income on housing or lives in a severely inadequate unit. Meanwhile, approximately 200,000 affordable housing units have been lost to the market during the past 5 years, and another 544,000 Section 8-assisted units are at-risk of loss during the next 5 years.

As we struggle to create more housing in this country, more affordable housing, we certainly cannot afford to lose any more of our existing affordable housing stock. It is much cheaper to preserve an existing unit of affordable housing than it is to build a brand-new one. In Rhode Island, a new housing unit can cost between $150,000 to $165,000 to build, while preserving an existing unit only costs between $50,000 to $60,000. So why are we here today?

We are here today because in many cases HUD is just letting affordable housing stock slip away. In my own State of Rhode Island, affordable housing groups and tenants have been struggling for over a year to keep 430 units of housing long-term affordable. I am concerned that HUD has been a hindrance instead of a help. So instead of enforcing rules requiring that tenants be given 1-year notice by the owner that the building is leaving the HUD Section 8 program, HUD allowed the owner to opt-out and even rewarded the owner with enhanced vouchers for all of the existing tenants. Despite a lawsuit brought by the tenants that resulted in an agreement that the owner would not prepay his mortgage for a certain period of time, HUD recently sold the mortgages on three of the

buildings to a bank in Texas without FHA insurance. This one action by HUD, whether intentional or otherwise, has effectively erased the recent State court settlement that would have kept these units affordable over the long-term.

In some cases, HUD has gone beyond mere neglect of its duty to preserve housing to outright hostility. HUD recently announced its intention to allow all owners of Section 8 project-based buildings who have refinanced to opt-out of their housing assistance payments, the HAP contracts, the very contracts that provide Section 8 subsidies to properties. Not surprisingly, over the past decade many owners have refinanced their original mortgages to take advantage of better interest rates. They have done so with HUD's approval and with the belief by all parties that the HAP contract remained in force.

HUD is now saying that, upon refinancing, the HAP contract terminates and that HUD intends to contact every owner who has refinanced to give them the opportunity to opt-out of their contracts and affordability restrictions.

I am very concerned with this decision by the Administration that could lead to a loss of 100,000 affordable housing units and look forward to discussing this issue with the Secretary today.

Today, we will hear from two panels of witnesses. The first panel will consist of Dr. John Weicher, Assistant Secretary for Housing and Federal Housing Commissioner, Department of Housing and Urban Development. The second panel will consist of: Mr. James Grow, Staff Attorney, the National Housing Law Project; Ms. Kit Hadley, Commissioner of Minnesota Housing Finance Agency; Mr. Tom Slemmer, President & CEO, National Church Residences; and Ms. Louise Sanchez, President, National Alliance of HUD Tenants.

Each of our witnesses has been asked to testify about affordable housing preservation issues, HUD policies that affect the preservation of affordable housing, and any proposals that should be considered as part of Federal legislation to encourage the preservation of affordable housing.

Before we begin, I would also like to thank each of you for your written testimony, which has been shared with all the Members of the Housing and Transportation Subcommittee, and I would ask that you stick to our 5-minute time limit for oral testimony so we may have more time for questions and discussions. I look forward, obviously, to this hearing.

When Senator Allard arrives or my colleagues, I will interrupt and allow them an opportunity to make an opening statement if they choose. Now let me recognize our first panel, Secretary John Weicher. Secretary Weicher is the Assistant Secretary for Housing and Federal Housing Commissioner at HUD. Prior to his appointment, he was the Director of Urban Policy Studies at the Hudson Institute.

Secretary Weicher, welcome.

STATEMENT OF JOHN C. WEICHER
ASSISTANT SECRETARY FOR HOUSING AND
FEDERAL HOUSING COMMISSIONER
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

ACCOMPANIED BY ROBERT S. KENISON
ASSOCIATE GENERAL COUNSEL
ASSISTED HOUSING AND COMMUNITY DEVELOPMENT

Mr. WEICHER. Thank you, Chairman Reed, and thank you for inviting me to testify this afternoon.

I would like to start by describing several initiatives of the Department to increase the available inventory of affordable housing before turning to the subject of preservation.

As you know, the FHA's basic multifamily housing insurance program is Section 221(d)(4). In the fiscal year that just ended, that program enjoyed a very substantial increase in activity. FHA made commitments for 198 new construction or substantially rehabilitated projects, with over 38,000 units and totaling $2.8 billion worth of mortgage loans. That total dollar figure is easily the highest for the program in the last 10 years. It is almost double our activity in fiscal year 2001 when FHA made commitments for 139 projects, with 21,000 units totaling $1.5 billion. That amounts to a 42 percent increase in the number of projects, a 79 percent increase in the number of units, and an 85 percent increase in the dollar value of commitments.

One major reason for this dramatic increase is that, in fiscal year 2002, HUD was able to operate Section 221(d)(4) on a self-sustaining basis. By raising the mortgage insurance premium to 80 basis points, we were able to end the program's dependence on credit subsidy. The industry doesn't need to be concerned anymore about program delays and stoppages because of credit subsidy issues, and three times in the last 8 years, FHA had to discontinue its credit subsidy program operations because we ran out.

I know that many people in the industry were concerned that raising the premium would cripple the program. Clearly, that did not happen.

Having put Section 221(d)(4) on a self-sustaining basis, the FHA is now in a position to reduce the insurance premium to 57 basis points, which will make the financing of new or rehabilitated apartments more affordable. The reduction is a result of a comprehensive review of the credit subsidy calculations for all FHA multifamily programs, the first such analysis in a decade.

You may recall from my confirmation hearing that I made a commitment to conduct this study. FHA completed it in time for the new credit subsidy calculations and the new premiums to be included in the President's Budget for fiscal year 2003 and to go into effect at the beginning of this fiscal year. We have lowered the premium on several self-sustaining programs, and we have lowered the credit subsidy rate on almost all of those that still require credit subsidy.

There are other reasons for the sharp rise in commitments. Shortly after he came to HUD, Secretary Martinez announced his support for a 25 percent increase in the statutory per unit limits for the FHA's multifamily mortgage insurance programs. This was the first increase since 1992. It helps make FHA more feasible in high-cost areas where the programs have not been used in several years. Philadelphia, for instance, has seen its first FHA-insured project in more than 5 years. Applications have been submitted for projects in Washington, in Baltimore, in St. Louis, and in suburban

Minneapolis, projects that would not have been submitted without the increase in the limits.

I also want to touch briefly upon some of this Administration's budget proposals that will increase access to or add to the current inventory of affordable housing.

The Administration's Budget for this fiscal year includes an additional $200 million in funding for 34,000 vouchers, in addition to the 1.74 million vouchers currently being utilized by low-income families. The Senate Appropriations Committee only provided funding for 17,000 new vouchers, and the Administration strongly urges Congress to fully fund our request.

Although the national vacancy rate is close to an all-time high at 8.5 percent in the second quarter of this year, there are still areas of the country with a low vacancy rate. To address this problem, the Administration also supports the development of affordable housing through the Low-Income Housing Tax Credit, which supports about 100,000 new or rehabilitated rental units each year. Two years ago, Congress enacted a 40 percent increase in the volume limits for the Tax Credit, and caps for tax-exempt housing bond financing were also raised last year. States can direct these resources to the local markets where supply is constrained or rents are highest.

In addition, the Administration has asked for increased funding this year for the HOME block grant of $1.8 billion. At that level, HOME will produce 23,000 new affordable units and a similar number of rehabs. The provision of these units will be made through decisions by local governments concerning their own affordable housing needs. Families with extremely low incomes will occupy over half of them. By law, voucher holders have access to all units developed with HOME and/or tax credit support.

I would also like to report progress on one of the first initiatives I undertook after becoming FHA Commissioner to look at the pipeline in Sections 202 and 811. A report prepared for GAO had indicated that there were over 100 projects from 1992 to 1997 that had not reached initial closing. I directed our Office of Multifamily Housing to determine the status of these projects. We learned that the pipeline data was badly out of date. Of the 100 projects listed as being in the pipeline, 25 had cancelled—some of them years ago—and 18 had already closed. I then directed our staff to close as many of the remaining projects as possible, and I am pleased to report that we closed 30 of them.

At the end of fiscal year 2002, that pipeline is down to 26 projects, 1.3 percent of the 2,058 projects funded during the 6-year period. This fiscal year, I expect we will close or cancel those 26 unless they are in litigation. We have also been working on the other end of the pipeline. Last year, we brought 75 percent of 202 and 811 projects to closing within 2 years of funding. In the past, it has only been 60 percent, I understand.

Turning quickly to the subject of preservation, the Department is committed to preserving the existing stock of affordable rental housing. Working with Congress, HUD has been successful in a number of efforts to preserve the affordable housing.

The Department has implemented Mark-to-Market and Mark-Up-to-Market to provide opportunities for owners to make capital

improvements and the necessary repairs to ensure the units are decent, safe, and sanitary for the residents and to ensure the units remain affordable.

Since the inception of the Mark-to-Market Program, OMHAR has successfully closed debt restructurings on 571 projects, including over 46,000 units, all of which are now subject to 30-year Use Agreements. These properties were provided with over $62 million in escrows for repairs, and an infusion of approximately $40 million in immediate Reserve for Replacement deposits to increase long-term physical stability. In addition, OMHAR has processed contract renewals and reduced rents on over 120,000 units, resulting in annual savings of over $105 million.

The Mark-Up-to-Market Program, created in 1999, has been similarly successful. In its first 4 years, over 600 contracts have been renewed and 58,000 affordable housing units were preserved under this program. The Department has also renewed over 1,000 Section 8 contracts in the Section 202 program, with more than 80,000 affordable elderly and disabled units being preserved.

For all of the Section 8 project-based programs combined, during the last 4 fiscal years, a total of 10,695 Section 8 contracts were renewed and over 778,000 affordable housing units have been preserved.

In my testimony, I address a number of specific policy matters concerning preservation. I would like to conclude by discussing one of them in particular. This concerns the contractual provisions governing the term of HAP contracts on State HFA Section 8 projects when the projects refinance and the recent legal opinion issued by the Department's Office of General Counsel.

The Section 8 contracts in question were executed prior to 1980. They provide that the term of the contract terminates, and I quote, "on the date of the last payment of principal due on the permanent financing." It is my understanding that up until the recent OGC opinion, HFA's have interpreted the HAP contract language to mean that new financing is included as "permanent financing" and that the contract does not terminate when an owner refinances the original mortgage.

We recognize the concerns of project owners, State agencies, and Members of Congress about the potential consequences for the affordable housing stock. We share those concerns, and we have been discussing the situation and possible options with the Council of State Housing Finance Agencies.

Currently, in an effort to assure the availability of continued rental assistance for project residents, we proposed to the State agencies two alternatives for the affected project owners: First, the owner may elect to extend the maximum term of the HAP contract from the date of the prepayment so that it terminates at the originally scheduled maturity date on the permanent financing; or second, the owner may elect to renew the project-based Section 8 contract in accordance with the Multifamily Assisted Housing Reform and Affordability Act.

However, an affected owner could choose neither option and exercise the right to opt-out of the Section 8 contract. In this case, the owner must provide HUD and the tenants with the proper 1-year notice of HAP contract termination.

We will be continuing to discuss this important matter with the State HFA's and with others who are concerned.

This concludes my statement, Mr. Chairman. Thank you for the opportunity to appear before you, and I will be happy to answer your questions.

Senator REED. Thank you, Mr. Secretary.

Let me recognize my colleagues in order of their arrival. Senator Corzine, do you have an opening statement before we start a round of questioning?

STATEMENT OF SENATOR JON S. CORZINE

Senator CORZINE. Yes. Thank you, Mr. Chairman.

I, like you and others, believe that the preservation of affordable housing is one of the most pressing issues before this Committee. Often we talk about the need to build more affordable housing and neglect to highlight the amount of affordable housing that we have lost to abandonment, demolition, or the private market.

This is an extremely serious issue around the Nation, and I have to say it is a critical issue in the State of New Jersey. According to the Housing and Community Development Network of New Jersey, much of New Jersey's affordable housing is aging and at a risk of deteriorating to the point where it is no longer livable. The State has already lost much housing to the abandonment and demolition procedures. In a State that has the third highest housing costs in the Nation, further loss of affordable housing will only exacerbate an already dire affordable housing shortage.

Mr. Chairman, as you noted, HUD has actively taken actions to reduce the preservation of affordable housing. I wish I could say that HUD was actively assisting our State to preserve this housing. Last February, HUD foreclosed on a Section 8 project-based residence in Newark, New Jersey, the Brick Towers Apartments. Actually, this is quite a controversial spot in my community. Fearing demolition of their homes, residents of the Tower worked to secure private financing for a proposal to rehabilitate the property at no cost to the Federal Government. Despite their efforts to save their home, which contains 320 units of affordable housing, and their efforts to save the Federal Government the $12 million HUD plans to spend to demolish the property, HUD refused to even meet with the Brick Towers residents to discuss their concerns about the demolition or to consider the rehabilitation proposal.

I wrote to the Secretary numerous times requesting such a meeting, and to my knowledge, HUD has never met with the residents. And I find, as you can imagine, it extremely troubling. At the very least, HUD has a responsibility to listen to the concerns of those who are living there and are going to be disrupted.

Mr. Chairman, I also am concerned about HUD's reinterpretation of Section 8 Housing Assistance Payment contracts to allow owners of Section 8 properties who have refinanced their mortgages to opt-out on those Section 8 programs. Over the last decade, as you are aware, almost 200,000 affordable housing units have been lost to mortgage prepayments and opt-outs. HUD's new interpretation, in my view, will only serve to increase the loss of affordable units.

I hope that HUD is in the business of expanding access to affordable housing, not eliminating it. I look forward to hearing the testi-

mony of our panelists and, in particular, Commissioner Weicher's response to these concerns.

Senator REED. Senator Carper, do you have a statement?

COMMENTS OF SENATOR THOMAS R. CARPER

Senator CARPER. I do, just a brief one, if I could.

Mr. Chairman, thanks so much for holding this hearing and for a whole series of them focusing on affordable housing in this Congress. Some of those earlier hearings have shown that affordable housing continues to be a problem in our part of the country, and I think throughout the country.

My hope is that in the next Congress we will be able to develop a comprehensive approach to solve the affordable housing crisis or begin to solve the affordable housing crisis. Under your leadership, Mr. Chairman, I am confident that we will.

In the meantime, it seems that the least we can do is to preserve the affordable housing units we already have, and I am concerned about some recent regulatory actions that seem to work against preservations, in particular, HUD's recent legal opinion that would give certain Section 8 project owners the ability to opt-out of the Section 8 program if they have refinanced their mortgages.

Again, Mr. Chairman, we thank you for scheduling this hearing, and I want to say special thanks to our witnesses for being here.

I am supposed to preside at 3 o'clock, so I won't be able to stay for as long as I would like, but I wanted to be here for the budget.

Thank you.

Senator REED. Thank you very much, Senator Carper.

Senator Akaka, do you have an opening statement?

COMMENTS OF SENATOR DANIEL K. AKAKA

Senator AKAKA. Thank you, Mr. Chairman, and I appreciate your conducting this hearing today.

There is a severe nationwide shortage of affordable rental housing. Affordable housing units declined by 9.5 percent between 1985 and 1999. Hard working Americans are being forced to spend more than they can afford to find adequate housing.

The 2002 Report of the Millennium Housing Commission cited that one in four American households reported spending more than 30 percent of their income on housing in 1999. In my home State of Hawaii, affordable housing can be particularly difficult to find. According to the National Low Income Housing Coalition's annual Out of Reach Report, the average U.S. employee must make nearly $14.66 an hour to be able to afford a modest two-bedroom rental and be able to pay for food and for other basic needs. The Report indicated that in Hawaii a worker must earn $16.74 per hour. The median wage in Hawaii is $12.72 per hour.

The current limited existing stock of affordable rental units is likely to decline further as housing prices in particular regions continue to increase significantly.

HUD must take an active role in preserving existing affordable housing units. And HUD appears to be accelerating this decline in rental units. Like several of my colleagues on this Committee, I am extremely concerned with HUD's housing preservation policies. In particular, I am concerned that HUD's interpretation of Section 8

Housing Assistance Payment contracts allows owners of Section 8 properties to opt-out of the Section 8 program if they have refinanced their mortgages. This action is likely to drastically reduce the number of affordable units available. According to HUD, 180,000 units could be impacted by the implementation of this policy. In addition, this action could damage the creditworthiness of State Housing Finance Agencies' bond programs.

Mr. Chairman, I thank you for conducting this important hearing today, and I look forward to a complete examination of HUD's activities as they pertain to housing preservation. I want to thank the witnesses for appearing today. Thank you, Mr. Chairman.

Senator REED. Thank you, Senator Akaka.

Mr. Secretary, let's go right to the HAP contract issue because, as you know, it has elicited a great deal of concern. I find it terribly troubling.

First, how many units are affected by this reinterpretation?

Mr. WEICHER. We are counting it by projects, Mr. Chairman. We have 600 projects that we know of, and it may be up to 1,400 projects. We are still counting that. We estimate, if it is 1,400 projects, it will be a little over 100,000 units. So it is not as high as Senator Akaka was suggesting. I am not aware of a number from HUD in that range at all. I understand it to be possibly a little over 100,000 units. Among other things, we are trying to make sure we have a count on the possibly affected properties.

Senator REED. When you get that final determination, could you share it with the Committee?

Mr. WEICHER. We will be glad to.

Senator REED. I would make the obvious point: 100,000 units in a very tight market for affordable housing is a significant impact.

I just want to understand what went on here. For 20 years, the contracts have been interpreted as not being changed by refinancing. And then suddenly, HUD looks over 20 years of practice in which each time one of these refinancings took place, HUD had to approve the refinancing, and declares that for 20 years they have been grossly misinterpreting the contract. Is that what happened here?

Mr. WEICHER. No, Mr. Chairman. But let me say that I am not a lawyer, as you know, and this concerns a legal opinion. I have asked our Associate General Counsel for Assisted Housing and Community Development to come with me today, Mr. Robert S. Kenison, and with your permission, I would like to ask him to respond to the legal issues here.

Senator REED. Surely.

Mr. KENISON. Good afternoon, Mr. Chairman.

Senator REED. Good afternoon.

Mr. KENISON. I think your framing of the issue is pretty close to the facts as they have occurred. The only quibble I would take is that I do not think this is a HUD reinterpretation. Just let me say what I mean by that.

We were asked last spring by an attorney representing some owner, I believe in New Jersey, what the meaning of that contract was. This is in the Section 8 contract, which is limited to the State Housing Agency Program. The other Section 8 contracts for new construction and substantial rehabilitation that were prominent in

the 1980's and that make up the great majority of Section 8 project-based assistance do not have this provision in it. But we were asked to say what we thought this particular provision meant. Again, as Assistant Secretary Weicher said, this is a provision that was in what we call "the old reg contracts," those that were executed roughly from 1975 to 1980. And the provision called for the termination of the HAP contract on the shorter of two dates: A number of years certain that was written in, or on the last payment due under the permanent financing.

If the permanent financing permits a prepayment, that doesn't mean it is due on the last scheduled date of the original permanent financing. It means it is due when the permanent financing is completed, and that is when the HAP contract would terminate.

Everything you have said about what has happened in HUD participation and refinancing is accurate. I think no one looked at that contract before, and when we saw the case this time—and I believe a good resolution was made in New Jersey. But, nevertheless, that is the way we took it to read.

Since that time, the National Council of State Housing Finance Agencies has been very helpful in working with us, calling attention to much of what has happened in the past in refinancing the field, and clearly, I think what we have to say is that it has been understood or at least assumed that the contract did not terminate, notwithstanding this recent look we have taken.

Our look this time was reinforced by the fact that in 1980, when we developed and issued a new form of contract, that particular contract said that the HAP contract would expire upon the shorter of the number of years written into it or the date of the originally scheduled permanent financing maturity. It was a clear change from what we had before, and that is why we think this is problematic contract language.

We share your feeling about it 100 percent, but it is awkward, uncomfortably stark language.

Senator REED. Well, it is awkward language that has been followed for 20 years, and a certain—and I am an attorney, and we can argue about this endlessly. But it would seem to me 20 years of practice in interpreting any contract, particularly in literally hundreds of refinancings, in which the developers were represented by sophisticated counsel in most cases—not all—and this issue was never raised in 20 years?

Mr. KENISON. The exact meaning of that contract never was raised expressly. I think people assumed that the answer was it was okay.

Senator REED. I think if enough people assume the answer is okay, that might be the answer.

Mr. KENISON. For that reason, we would say that everything that has happened in the past is in the nature of what is called an implied contract.

Senator REED. That is true. And I think the implied contract can be enforced, just as these implied contracts. You have eliminated or given the developers the option of disregarding the contract. Are you prepared to go in and recoup the payments that were made under these contracts?

Mr. KENISON. No. Certainly we would argue that that implied contract lives up to today and everything that was paid, they get the benefit of the deal.

Senator REED. Then why would suddenly this implied contract in which the regulations apply be nullified on one side and not the other?

Mr. KENISON. Now that this issue has been focused on and we think the meaning of the contract is so clear, we think it would be helpful to prospectively make that clear by amendatory contracts.

Senator REED. But you are giving the choice to the developers. If they choose the best option for themselves, that is fine. But you prejudice tenants who are living in these units.

Let me also just say that I think clearly this could be easily interpreted the other way, and you have chosen an interpretation which I think defies 20 years of practice. But a specific question: Who was the individual and what entity did he represent who sought this reinterpretation?

Mr. KENISON. I don't know. The attorney was Mr. Levy on behalf of a project in New Jersey. I can find that out.

Senator REED. Could you give us that information?

Mr. KENISON. Certainly.

Senator REED. So one lawyer, one project, by inquiring to your office caused you to change the practice that was in place for 20 years that has been essentially abided by and unquestioned by legions of lawyers over that 20 years?

Mr. KENISON. Well, I think there may have been other inquiries. I don't know. But this was the first time the question was so explicitly put.

Senator REED. I find it mind-boggling.

Mr. KENISON. Yes, I——

Senator REED. You know, part of being a lawyer is coming up with solutions that are fair and sensible and consistent with practice, and I do not think you did.

Senator Corzine.

Senator CORZINE. Mr. Weicher, does HUD plan to conduct an analysis of availability of affordable housing with respect to 325 Brick Towers Apartments, if you are familiar with that, and its impact if we demolish it in Newark, which is, as I stated in my opening statement, a very serious concern for the community?

And on a more general basis, are there any standards that HUD uses when determining whether or not to allow such housing to be demolished or preserved?

Mr. WEICHER. Senator Corzine, as I am sure you know, we have sold the project to the Newark Housing Authority, and we have sold it with rental affordability deed restrictions. And if the project is demolished and new housing is constructed, then there are those affordability restrictions. The residents would receive vouchers to enable them to find other housing not just within Newark, but also within New Jersey, and for that matter Northern New Jersey, and beyond.

If I might say in response to your earlier opening statement, early in the process HUD did meet with the residents and discussed with them the plans to sell the project to the Newark Housing Authority, and at one point the residents were invited to put

together a proposal for the project, and they did not. My understanding is that they did not express interest in doing that. We therefore signed a contract, an agreement, gave an option to the Newark Housing Authority, and it is on that basis that the recent sale occurred.

The last request that we received to meet with the tenants, we were advised that because of the litigation of that building, General Counsel for that matter at the Department of Justice advised us not to meet with the tenants, and therefore we did not. We did request that the Newark Housing Authority meet with the residents about the sale.

Senator CORZINE. Did you follow up whether they did?

Mr. WEICHER. Yes.

Senator CORZINE. And did the Newark Housing Authority meet with them?

Mr. WEICHER. Yes. I am sorry. Let me just correct that, Senator Corzine. A meeting is planned.

Senator CORZINE. It is my impression that there has been no meetings, at least from the September time frame onward.

I think while it is important for the local residents in this particular situation, I think it is indicative of the real problem that we have here, because for the citizens that live here in this housing project, there is virtually no available use of vouchers. Vouchers are going unused because of lack of availability in Newark, and so we are now creating a situation where people have to, as you described, move somewhere in the State of New Jersey or potentially outside of the State of New Jersey, while they may have jobs with limited transportation opportunities in and around the area.

I think it is descriptive of a problem that is extraordinarily difficult for a lot of the people that live in affordable housing, particularly in States which have such a dramatic shortage of affordable housing, and I am concerned that all of us, not just HUD, but all of us together are not being sensitive enough to the availability of housing and taking those steps that move in the direction of at least maintaining what we currently have in place on a commonsense basis. And demolition in this particular instance, particularly when there was another developer willing to come in, we have not been able to have the kind of dialogue on a consistent basis.

I have sent two letters to Secretary Martinez with regard to this issue, and I continue to be very concerned about the lack of real engagement with regard to resolving the number of affordable housing units in Newark broadly, which I think is representative of the Nation.

Mr. WEICHER. Senator Corzine, I might just comment that there is statutory right of first refusal for State and local entities when we acquire a project and are prepared to sell it. Newark Housing Authority had that statutory right and exercised it. During all of the vicissitudes of discussion within Newark, that right remained available to them.

I might also say that we are committed to preserving the available stock as much as we can. As I said in my statement, in the last 4 years in a variety of programs, we have preserved close to 800,000 units, about 778,000 units over that period of time, and

that is a very substantial share of the inventory, the total inventory, not just the inventory that came up for renewal.

Senator CORZINE. I just reiterate that that may be on some macro level. In a lot of the most desperate need areas of our urban communities, where affordable housing is in its most minimal supply, that does not appear to be the case, certainly not in Newark, certainly not in Camden, where I could go back and recite other elements of similar kinds of actions, and I think that their response with regard to vouchers really is indicative of what I am concerned about, which is an indifference in making sure we have adequate numbers of affordable housing.

Senator REED. Thank you, Senator Corzine.

Senator Akaka, and then we will recognize Chairman Sarbanes.

Senator AKAKA. Thank you very much, Mr. Chairman.

Secretary Weicher, Section 613 of the Mark-to-Market Extension Act required HUD to establish procedures to ensure that rents offered to owners as an incentive for participation in the Section 8 program, these incentives are to be comparable to the enhanced voucher rents, supported by the public housing authorities and Federal subsidies, when their owners opt-out. What is HUD doing to comply with this requirement?

Mr. WEICHER. The requirement to provide enhanced vouchers to residents who may be affected by the decision to prepay a project and not to keep it as affordable housing? We are providing these enhanced vouchers to the residents in those projects, and the enhanced voucher means that they can stay in the project at the rent that the landlord is charging. This requires the local approval of the PHA for that rent, but they can stay in the project at that rent, or they can use the voucher at the fair market rent for the local area, and they can use that voucher anywhere else in the local area. So, we are providing enhanced vouchers which I think was one of the most useful ideas to break the tremendous impasse that existed in Congress and in Administrations about preservation for over a decade, and we are doing it.

If you are aware of instances where residents are saying they were not provided with enhanced vouchers, then we would very much want to know about those instances.

Senator AKAKA. Several of our witnesses in their testimony have suggested that HUD create an office of preservation to better coordinate its preservation efforts. What type of coordination of efforts currently exists within HUD and how can these efforts be improved?

Mr. WEICHER. We have, of course, the Office of Multifamily Housing Assistance Restructuring, which is responsible for both the Mark-to-Market Program and the Mark-Up-to-Market Program, and that includes all of the Section 8 properties, which are the vast bulk of what is at issue here. With respect to the other properties that would be involved would be Section 236 projects. There are not very many of those, and those are handled through the regular program office. I do not have any sense that we need a different structure than we have.

Last year Congress, in reauthorizing OMHAR, placed OMHAR within the Office of Housing, with the Director of OMHAR reporting to me, rather than being independent of the Department essen-

tially and reporting to the Secretary, and that has improved our ability to coordinate our activities. There is a close working relationship between the Office of Multifamily Housing, basic FHA and Sections 202 and 811 programs, and the Office of Multifamily Housing Assistance Restructuring. I meet with the Director of that office weekly, and sometimes more than weekly, and he is meeting with the Office of Multifamily Housing, the staff is meeting with the Office of Multifamily Housing regularly, and it seems to be everyone's sense that this is working better than the previous arrangement had worked.

Senator AKAKA. Mr. Secretary, how will HUD utilize its authority for Interest Reduction Payments on certain terminated and recaptured Section 236 properties with IRP contracts, which are used for the rehabilitation of multifamily projects?

Mr. WEICHER. The Emergency Supplemental Act, this summer, rescinded $300 million that had been estimated in the budget, for Interest Reduction Payments. That took all the money that we had for that program. Looking forward, we have in the budget for 2003 a $100 million estimate. That is an estimate. What actually happens depends on a number of factors. We cannot really know how many projects we will choose to prepay in the course of the year. Some of the projects, we will be able to decouple the IRP in the sense they will continue to receive the Interest Reduction Payments in return for agreeing to affordability restrictions when they refinance, and some projects will Mark-Up-to-Market and not, therefore, opt-out, and the Interest Reduction Payment will not come into play.

There is also a complication in that the contracts prepay, that the money becomes available over the course of the fiscal year, and we cannot know the timing of that, and we have to make the commitment to begin the program, make the funds available before the end of the fiscal year. So if we assume we get $100 million this year, and again it is not rescinded, then it will be a question of the timing at which the money will become available. If the recision had not occurred, we were working on a feasible program with the money that we had available, and we still could, but we have no money at all.

Senator AKAKA. Thank you, Mr. Secretary.

Senator REED. Thank you, Senator Akaka.

Senator Sarbanes.

COMMENTS OF SENATOR PAUL S. SARBANES

Senator SARBANES. Thank you very much, Mr. Chairman. I am sorry I was not able to be here at the outset, but this is a busy time of the legislative session.

First of all, I want to thank Chairman Reed for holding this very important hearing. Obviously, preserving affordable housing already in stock is a very critical issue. The National Low Income Housing Coalition released its annual Out of Reach Report just a few weeks ago. There is not a city or county in the country where a full-time minimum wage earner can afford to put his or her family in a two-bedroom apartment. In fact, on average, a worker needs almost $15 an hour to pay for modest housing, almost three times the minimum wage.

These figures make it very important that we preserve what affordable housing we have. It seems to me that HUD should be very much involved in that endeavor. Regrettably, and I know we will hear about this from the other witnesses to follow, HUD seems to be undercutting efforts to preserve affordable housing, either through indifference and inaction, or sometimes just a hostility to innovative ideas, a hostility that seems to me to be more driven by ideology than by common sense.

Having said that, I want to ask some questions of the Secretary.

I may touch on subjects that have been covered to some extent. On August 29, quite some time ago, Senator Reed and I wrote to the Secretary about the reinterpretation of Section 8 housing assistance payments contracts in a way that would allow owners of Section 8 properties to opt-out of the Section 8 program. It was our understanding, as we raised then, that the reinterpretation applied not only to projects that refinance in the future, but also to any projects that had refinanced in the past. So that is the first question I want to ask.

First of all, presumably this letter was referred on to you, Mr. Secretary?

Mr. WEICHER. I am sure it was, Senator. We are the logical people to be responding to it. I am surprised if you have not received a response, and I will certainly look into that.

Senator SARBANES. Fine. That is the first question I want to ask. This is October 9. We sent this letter on August 29 on a matter we think is of some importance and we have gotten no reply.

Mr. WEICHER. I will look into that. I can tell you that the Department tracks Congressional correspondence very carefully, as do I. And to my knowledge, we have no overdue letters from any Member of Congress, and we have certainly had no overdue letters since well before the date of your letter, and we track this every week. The deadlines are weekly and we track this every week. I will look into that and give you a specific time.

Senator SARBANES. Well, let us go to the substance.

Mr. WEICHER. Excuse me, Chairman Sarbanes. With me is our Associate General Counsel for Assisted Housing and Community Development, who is knowledgeable about this whole issue, and essentially it is an issue of a legal opinion, and Mr. Kenison might have something to say about that letter I believe.

Mr. KENISON. Mr. Chairman, I just wanted to say that that letter, because of the source and the importance of it, was directed to be prepared for the Secretary's signature. My office prepared a letter. It is in clearance and should be out very quickly.

Senator SARBANES. Where is the letter? Do you have it with you?

Mr. KENISON. No.

Senator SARBANES. Mr. Secretary, let me just ask you about the policy? What is going on? I am told, even by your own estimates, 180,000 units, affordable housing units, could be lost under this new policy.

Mr. WEICHER. Mr. Chairman, Senator Akaka made reference to that number also, and the count that we have is that something over 600 projects, perhaps as many as 1,400 projects, may be affected. If it is 1,400 projects, it would be a little over 100,000 units that would be affected. I do not want to minimize that, but if you

have other numbers from HUD, I certainly would want to see them, because we have been working very seriously on this issue. We recognize it as a problem. It was called to our attention unexpectedly, as Mr. Kenison said, early, by either a developer or an agency in New Jersey—he can respond to this—and we realized immediately that we had a problem here, and we have been working to try to identify a solution. We have met with the Council of State Housing Finance Agencies. We know their concern. We know the concerns of the Members of Congress. We share those concerns. We are trying to work out a solution that is legally appropriate.

Senator SARBANES. Well, what kind of solution are you trying to work out?

Mr. WEICHER. What we have done is we have offered options to owners to renew the contracts on these projects that have already been—the contracts were terminated and refinanced. We have been working to make sure that option is available.

Senator SARBANES. Have you opened up all the past contracts?

Mr. WEICHER. It is not all of them.

Senator SARBANES. For refinancing?

Mr. WEICHER. It is not all of them. It is the contracts which were State Housing Finance Agency projects and the contracts were executed prior to 1980. That is why it is between 600 and 1,400 projects and we have a total universe of Section 8 projects of about 15,000.

Senator SARBANES. Didn't HUD assent to these refinancings?

Mr. WEICHER. May I, at this point, refer to Mr. Kenison as the legal expert on this?

Senator SARBANES. Well, except there are important policy implications, but let me just hear him, yes.

Mr. KENISON. I think that is a fair way to ask the question, Mr. Chairman, and, yes, HUD did assent to them.

Senator SARBANES. Did you not continue to pay funds to Section 8 property owners who did the refinancing?

Mr. KENISON. Correct.

Senator SARBANES. Now, you are coming back and saying that they are out of their obligations to keep the housing affordable?

Mr. KENISON. What we are saying is no one had ever looked at the contract provision before. The contract provision is painted in very bold language that throws into question what we have done. There is no question, however, but what has happened in the past, the practice has been total assent to the refinancing. That is why the package now, described by Assistant Secretary Weicher, tries to get them all up to speed in accordance with the contract language and practice.

Senator SARBANES. My understanding is that the State Housing Finance Agencies, which finance many of the properties, and the building owners, had all interpreted the language to mean that new financing is included in permanent financing, and the contract does not terminate when they refinance the original mortgage.

Mr. KENISON. That is what my understanding——

Senator SARBANES. They refinance the original mortgage in order to get a lower interest rate, right?

Mr. KENISON. Yes, sir.

Senator SARBANES. And that is to the advantage of the owner, is it not?

Mr. KENISON. Sure.

Senator SARBANES. But now you are telling us that because that has been done, and that was permitted, that they are now out from under their affordable housing obligation?

Mr. KENISON. We are saying that they have the option of formalizing what has been happening in practice for the last 15 years by executing an amendatory contract.

Senator SARBANES. Suppose they refuse to do that? Then they are out from under the restrictions?

Mr. KENISON. We think that is a problem.

Senator SARBANES. How do you reach a conclusion like that in light of the fact that this has been a standard practice and has been accepted by everybody?

Mr. KENISON. There is a vast tension between that accepted broad practice and the words that are in the contract. That is why the National Council and State Housing Agencies have proposed legislative language, and we have looked at that, and given them a technical drafting service.

Senator SARBANES. Everyone is desperate to prevent the loss of this housing, but the whole problem originates from a HUD interpretation.

Mr. KENISON. Yes, sir.

Senator SARBANES. Secretary, you are against Section 8 project-based, are you not?

Mr. WEICHER. Mr. Chairman, we are managing the Section 8 inventory in accordance with the statute. We are committed to preserving the units that were subsidized in the period between 1974 and 1983, and for that matter the earlier units under Sections 236 and 221(d)(3)BMIR. This is not an issue of ideology. We know what the law is. We are following the law. We have devoted a lot of effort to preserving the stock.

I mentioned in my opening remarks that over the last 4 years we have preserved close to 800,000 units in Section 8 through Mark-to-Market, Mark-Up-to-Market, and the 202 projects that had Section 8 contracts, and we are continuing to work on that. We work very closely with OMHAR. My Office of Multifamily Housing works very close to OMHAR. This is a legal interpretation, which as Mr. Kenison said, the issue arose as a surprise to all of us in the Department. We have all been proceeding on the basis that these earlier HAP contracts continued, as Mr. Kenison said, for 15 years. I do not know the period of time, but this came as a surprise. The General Counsel's Office spent some time on the issue before reaching that conclusion.

Senator SARBANES. We need an answer to our letter. I want to see the opinion, but this is an outrage. You could lose, by any estimate, over 100,000 units of affordable housing, and you are sitting there telling me that it is a legal interpretation of a practice that has been prevailing and to which everyone has assented and has participated.

Mr. WEICHER. Mr. Chairman, I do not want to minimize at all the extent of the problem.

Senator SARBANES. No, I hope not.

Mr. WEICHER. I would say that we do not have any expectation that over 100,000 units would, in fact, opt-out. There are a number of States, including some large ones, in which State provisions discourage prepayment and opting-out, discourage opting-out, and we do not have any reason to believe that all of the owners who are affected would choose to opt-out.

Having said that, because I think it is important to give you the best information we can, again, I do not want to minimize the extent of the problem. We are very concerned, and we recognize that this is completely unexpected by all of us.

Senator SARBANES. I am interested because I was involved with some of my colleagues in trying to preserve affordable housing. HUD would not allow the transfer of Section 8 subsidies to replacement housing as part of a broader revitalization plan to build mixed-income housing in Pittsburgh and Indianapolis; correct?

Mr. WEICHER. The statute does not permit what the developer wanted to do in Pittsburgh and Indianapolis, which essentially was to transfer Section 8 project-based subsidy to newly constructed projects. The Administration does not favor that, and opposed doing so. We worked out an agreement with each city, separate agreements with each city, similar, but there are some legal differences between the project status. We worked out an agreement with each city, under which the city would be able to take title to each of the projects affected, and the city would receive substantial funding from us for demolition and redevelopment of housing on the sites on which those projects were located, which was consistent with our legal authority.

Senator SARBANES. Did you oppose a legislative proposal to alter your legal authority in order to permit this to happen?

Mr. WEICHER. The Administration did not—there was an amendment proposed to the Appropriations bill last year. We were opposed to that. We met with Members of this Committee, and we agreed that we would not oppose that amendment. It did not make it into the Appropriations bill, which frankly, I did not realize until after the Appropriations bill was signed and published. We subsequently learned that there was opposition with the House, as well as when the issue was reopened by the cities. There was opposition within the House to the original amendment, and continuing opposition to the legislative change, and there was opposition by the Administration to a legislative change. And on that basis we worked out an agreement with the cities and with the developer, and to our knowledge, those agreements are what we are operating on, and we intend to abide by them, and we think that those agreements solve the problems that the cities are concerned with and that the developer is concerned with within our current legal authority. We intend to go forward and continue, as we have been, to work with the cities to bring those projects to the conclusion that we have agreed on.

Senator SARBANES. Mr. Chairman, you have been very generous with the time, and I appreciate that very much. We obviously are just beginning to scratch the surface here, and I think this is an extremely important issue, and I must say I do not have any sense of any, not even asking for a mission, but any sort of a commitment on preserving affordable housing, which is unfortunate since I

think we look to HUD to provide some momentum for, and some leadership for, and some imagination. I am sure this is a matter we will continue to pursue.

Thank you.

Senator REED. Thank you, Chairman Sarbanes.

I have a few additional questions.

First, again, this issue of the HAP contracts is so intriguing. After 20 years of consistent interpretations by both sides, apparently one or two lawyers approaches HUD, claims, in a rather novel argument, that 20 years of experience and interpretation is absolutely wrong. HUD, on their own volition, changes the regulations and the policy. Was any thought given to resisting a possible lawsuit? Who made the policy decision not to test this policy of 20 years in court? That is not a legal judgment. That is a policy judgment. Mr. Secretary, did you make that judgment?

Mr. WEICHER. No. The Office of General Counsel concluded that the contract had not been interpreted correctly. That is the judgment of the Office of General Counsel. As you know, the General Counsel, like me, is a policy official of the Department. This Committee confirmed him at the same time that you confirmed me. And this is the opinion of the Department that we do not have that authority.

Senator REED. So after 20 years of practice, no lawsuit was initiated; is that correct, Mr. Kenison?

Mr. KENISON. Yes, Mr. Chairman.

Mr. WEICHER. That is correct.

Senator REED. No lawsuit was initiated. And suddenly you just throw 20 years of practice out. You do not even say, well, you know this is a close call. We have been doing this for 20 years. We would probably have a good argument in court. Mr. Kenison, do you think you would have a good argument in court?

Mr. KENISON. I think we would have a great argument for the money that has already been paid out, and the tenants who have been assisted to date. What would happen in the future I think is the problem.

Senator SARBANES. But your ruling went back, did it not?

Mr. KENISON. The ruling goes back to the fact that it affects the past, as well as the present. But insofar as any given owner has received assistance and gotten the benefit of the bargain, we would not challenge that.

From the——

Senator REED. But it is just—excuse me, sir. Go ahead.

Mr. KENISON. I was just going to say that from the standpoint of litigation, we considered that to a degree, that litigation would probably come against HUD by owners.

Senator REED. Well, there was no litigation by HUD by any owners, is that correct?

Mr. KENISON. Absolutely correct.

Senator REED. So how many issues are pending before HUD now that are being litigated because owners have disputed contracts?

Mr. KENISON. I do not know. Not a lot.

Senator REED. Not a lot?

Mr. WEICHER. I can——

Senator REED. But this was not important enough to test the seriousness of the claim by the developer community by saying, if you feel that is your interpretation, you have a right to go to court? This was seen so automatic and so unimportant that we just say, oh, sure.

Mr. KENISON. It was seen as extremely important, but it was seen almost as automatic. That language is so straightforward.

Senator REED. Twenty years of experience absolutely undercuts your argument, I am sorry. I appreciate the fact that you are advocating, and you study this issue more than I do, but I will stop.

Mr. KENISON. Mr. Chairman, I really do not mean to advocate. We just read that contract, and it reads very sparely that it terminates on the earlier of two dates; a number of years certain or the date on the last payment of the permanent financing.

Maybe one reason no one looked at that before, and I would not say it was interpreted, I would say it was always assumed that the contract survived, is that the vast majority of these project-based contracts, not with the State Housing Finance Agency do not have that provision in it. So if you go to refinancing or assignment of the contract, of course, it carries forward.

Senator REED. Again, one could make a very good legal argument that, by implication, if it is unclear, then the other thousands of existing HUD contracts would be controlling, at least by implication. We can get into a long legal argument, and I respect the fact that this is a legal issue, but it is just you did not even fight about it. And we always hear these, you know, we have to run Government like a business. I cannot conceive of any business who is questioned on an issue with this ambiguity, after 20 years of consistent interpretation, it may be because no one raised the issue, but consistently, and it is an important issue, whether they can get in on a contract. Every time these contracts, these refinancings came up, HUD looked at these contracts, at least perfunctorily.

Mr. KENISON. Well, and the State——

Senator REED. Yet this is just, well, we just fold up our cart.

It goes to the remedy, too. The remedy is basically whatever is the best deal for the developer. It is not preserving affordable housing. It is not even trying to preserve affordable housing.

Let me move to two other issues because I think the Secretary and you——

Mr. WEICHER. Mr. Chairman, could I just, speaking of the benefits to the owner, presumably the refinancing was done in order that the owner gained a benefit out of the refinancing, right? I mean, in financial terms.

Mr. KENISON. Sure.

Mr. WEICHER. In addition now, he has also gained this huge benefit on top of that by HUD's interpretation, so he can now walk out of his contract. So, you have to approve the refinancing, do you not?

Mr. KENISON. I am not sure if in the State finance program we approve them. I do not think we do. This is the program in which the State Housing Agencies were given the discretion.

Senator SARBANES. All right. They approve it. You have to continue to make the Section 8 payments.

Mr. KENISON. Sure.

Mr. WEICHER. Yes, Mr. Chairman.

Senator SARBANES. So, you approve it, he gets better financial terms, and now he walks away from his affordable housing obligation. Boy, that is a deal.

Senator REED. Mr. Secretary, two other issues if I could.

First, notice requirements for opting-out of Section 8. There are several examples in my State of Rhode Island, in Texas, and in Los Angeles, where individuals suggest that HUD has not enforced requirements for appropriate notice before opting-out of the Section 8 program.

In Los Angeles, the owner is alleged not to have abided by State notice requirements. That is something that HUD recognizes, but HUD says they will not get involved, but the question really is, what assurances can you give us that you are going to enforce the notice requirements?

Mr. WEICHER. Mr. Chairman, to my knowledge we are enforcing the notice requirement, and we certainly intend to enforce the notice requirement across the board. I would very much like to see any of the examples that you mention, any alleged examples, we will look into all of them. This is not our policy to stamp on that notice anywhere along the line.

Senator REED. We will make those references, but in the State of Rhode Island, we had a situation where we asked HUD to look into the issue of notice, and they refused to get involved. Tenants, I believe, went to court, got a State ruling, and then HUD, as I mentioned in my opening statement, decided to sell the mortgages to a bank in Plano, Texas, claiming now that they are no longer the responsibility of HUD. We will get the information to you.

Mr. WEICHER. Is this the three projects that you mentioned in your opening remarks?

Senator REED. In my opening remarks.

Mr. WEICHER. The owner did prepay on those, and there was no subsidy and no use restrictions on those at this stage. I understand the current question is, is the court settlement, and we were not party to that court settlement anywhere along the line.

Senator REED. We will provide specific details, but as I understand it, the issue was not the prepayment as much as the notice to prepay.

Mr. WEICHER. Please give us that information in as much detail as you can.

Senator REED. With respect to another issue, in Ms. Sanchez's testimony, she talks about enhanced vouchers and HUD's lack of enforcement ensuring that owners who opt-out accept enhanced vouchers. Do you have any knowledge where owners are refusing to accept enhanced vouchers after opting-out?

Mr. WEICHER. When we met with Ms. Sanchez and other leaders of the National Association of HUD Tenants, one or two people in the room mentioned problems with owners not accepting enhanced vouchers in their projects in their communities.

The information I was able to obtain at that meeting was that these were situations where the Public Housing Authority was not permitting the enhanced voucher to go to the maximum permitted, to the rent that was being charged on the project, but were setting a lower maximum for the enhanced voucher, which I understand is legally permissible.

Those are the only instances that I have been aware of, and if there are other instances, I imagine you are going to be sending me a lot of paper, but that is fine.

Senator REED. Thank you very much.

Senator Sarbanes.

Senator SARBANES. Mr. Chairman, I know we have a panel waiting, and I think we should hear from them. I just, again, want to thank you for holding this hearing, and I want to underscore the fact that I think it is very apparent that there is an area here crying out for a very careful Congressional oversight, and I am very pleased that you have here launched that effort, not concluded it, but launched it, and thank you very much.

Senator REED. Thank you, sir.

Thank you, Mr. Secretary. Thank you, Mr. Kenison.

Senator REED. Let me call the next panel forward, please.

I will call the second panel to order and introduce our witnesses.

Mr. James Grow is a Staff Attorney at the National Housing Law Project, Oakland, California. Jim is the Project's principal staff for HUD-assisted preservation work and has spent his legal career working on affordable housing issues. Thank you, Mr. Grow.

Ms. Kit Hadley has been a Commissioner of the Minnesota Housing Finance Agency since July 1994. Prior to her appointment as Commissioner, she served as the Deputy Commissioner and Director of Government Affairs.

Mr. Tom Slemmer is President and CEO of the National Church Residences in Columbus, Ohio. Founded in 1961, National Church Residences is one of the country's leading nonprofit organizations specializing in the development, construction, and management of over 1,400 units of affordable housing designed to serve the elderly, low-income families, and persons with disability through Federal and State grants, loans, and tax credit programs.

Ms. Louise Sanchez is currently the NAHT Board President and has been an NAHT Board Member since 1997. She also serves as a Co-Chair of the Mitchell-Lama Residence Coalition, which represents over 101,000 families in Mitchell-Lama subsidized developments in New York State.

We look forward to your testimony. Let me remind you, again, that your full statements are in the record, and I would ask you to abide by our 5-minute limit.

Mr. Grow.

STATEMENT OF JAMES R. GROW
STAFF ATTORNEY
NATIONAL HOUSING LAW PROJECT
OAKLAND, CALIFORNIA

Mr. GROW. Thank you, Mr. Chairman. Thank you for providing the National Housing Law Project with this opportunity to testify on the preservation issue.

Our organization provides legal and technical support to hundreds of tenant leaders, organizers, nonprofit organizations, and legal advocates throughout the country who are working every day to preserve affordable housing. We all do this work because of a shared commitment to the basic principle that everybody needs a place to call home, and that housing that is decent and affordable

or can be made so and provides stability against arbitrary eviction merits our special attention because once it is lost, it is virtually impossible to replace.

Our mutual experience demands that Federal policies and practices must promptly be reformed. My written testimony covers the recent history of Federal preservation policy, current problems, specific examples in greater detail, but in my remarks, I would like to focus on four major points.

First, since 1994, with only a couple of notable exceptions, Federal preservation policy has been in a full-scale retreat, but often a retreat that is wrought in total silence. Much of the harm has been made through budgetary decisions and related changes in law adopted through the appropriations process, with little public input from the normal legislative authorizing process.

Two prime examples of this backward procedure include: First, Congresses' abandonment of the Federal Preservation Program, in favor of authorizing unrestricted prepayments for properties with HUD-subsidized mortgages; and, second, with Congresses' adoption of so-called flexible authority, beginning in 1995 and made permanent a year later, giving HUD incredibly broad and standardless discretion over its decisions concerning properties with HUD-held mortgages or that are HUD-owned.

Thousands of units, formerly protected by Federal laws that were carefully crafted through the normal legislative authorizing process, have been lost without those laws ever having been revised or repealed.

My second point is that Congress and the public need to know much more about HUD's activities under its existing statutory and regulatory authority. Congress may not fully realize how HUD is interpreting, applying, or even ignoring statutes that it has passed. At various times over the past 30 years, and certainly for much of the past decade, HUD has been on a mission, not to preserve affordable housing, but actually the opposite, to get rid of it.

In pursuing this mission, HUD thrives on Congressional ignorance. When the harmful or illogical consequences of thoughtless agency decisions reach the light of day, the Congress has often responded on a bipartisan basis: For example, by enacting the Mark-to-Market Program in 1997 and by adopting the "Mark Up" and enhanced voucher protections that preserve more housing and protect residents a couple of years later in 1999.

Vigilant and persistent oversight, coupled with accurate data on critical issues from HUD itself, is essential to responsive preservation policymaking and administration.

My third point. Preservation policy should not be built around the concept of owner choice that underlies current policy on most prepayments and Section 8 opt-outs, nor should it rely on unbridled HUD discretion that governs HUD's activities concerning HUD-owned properties and those with HUD-held mortgages.

Congress should establish or reinstitute public policy criteria concerning the circumstances under which developments should be preserved or not, as was true under the 1990 preservation program and the 1994 property disposition policy.

Congress should also provide appropriate procedures and the funding to make preservation happen, possibly with participation

by State and local governments. Granting HUD discretion is extremely hazardous, even where HUD is directed to make specific findings, as in the case of those prepayments that still require HUD approval. This is especially dangerous when HUD is given discretion with no statutory criteria whatsoever, as in the case of the Flexible Authority statute, where HUD takes this as a license to ignore all prior unrepealed statutes and regulations such as those governing multifamily foreclosure and disposition activities and mortgage sales.

Congress may not be fully aware of what it did in 1995 because it was buried in an emergency supplemental appropriations bill and made permanent a year later, arguably allowing HUD to override all other existing statutes and rules.

I would like to echo your remarks earlier, Mr. Chairman, concerning HUD's recent mortgage sale of multifamily HUD-held notes which included those on several Rhode Island properties. This note sale may have stripped away all Federal regulatory protections such as budget-based rent restrictions and perhaps even prepayment restrictions. Certainly, it has made it a lot more difficult for residents to prevail on their legal challenge to the prepayment and opt-out under Rhode Island law.

That HUD would do this without identifying or analyzing the impacts of its actions on the preservation of affordable housing demonstrates a serious administrative failure, whether it is committed by HUD staff or by due diligence contractors.

My last point is that preservation policy cannot be driven solely by a desire to save Federal budget authority. Congress must reform its budget accounting rules or create exceptions that permit longer term subsidy commitments that do not increase actual annual outlay spending. This will enable the creation of appropriate preservation and rehabilitation policies—set a level playing field, if you will, to measure the costs of preservation with those of other options. But even so, cost-effectiveness is but one part of an overall process that must also evaluate both the feasibility and the social benefits of preservation.

We are paying high prices to protect tenants when owners prepay or opt-out under the enhanced voucher program, but the irony is we are not getting any housing preserved in the bargain.

The Federal Government should also commit additional resources to support the financial contributions of State and local governments through matching grant programs and to complement other Federal preservation tools, such as Mark-Up-to-Market in Section 8 and the targeted use of Federal Multifamily Mortgage Insurance to ensure preservation for nonprofit transfers.

Finally, one of the most important additional tools to advance preservation would be to adopt Federal income tax relief on the noncash gain for those owners that transfer properties at commensurately lower sales prices to tenant-endorsed nonprofit preservation purchasers, as recently recommended in concept by the Millennial Housing Commission.

Thank you, Mr. Chairman.

Senator REED. Thank you, Mr. Grow.

Ms. Hadley.

STATEMENT OF KATHERINE G. HADLEY
COMMISSIONER, MINNESOTA HOUSING FINANCE AGENCY
ON BEHALF OF THE
NATIONAL COUNCIL OF STATE HOUSING AGENCIES
WASHINGTON, DC

Ms. HADLEY. Chairman Reed, thank you for this opportunity to testify on behalf of the National Council of State Housing Agencies. Preservation of the existing supply of Federally-assisted housing is one of the most important goals of the Minnesota Housing Finance Agency. There are many critical preservation issues that need the attention of Congress and HUD in partnership with the States.

However, I would like to spend the rest of my 5 minutes on the preservation problem that did not exist until a few months ago. The problem is the opinion of the Office of General Counsel on HAP contracts that has been well-described by you.

We point out, as you have, that HUD has concluded that the HAP contracts terminated upon a refinancing, despite the fact that HUD itself approved the assignment of the HAP contract to the new financing in hundreds of transactions in State after State, year after year, despite the fact that HUD itself continued to pay Section 8 subsidies on hundreds of refinanced developments in State after State, year after year, and despite the fact that letters from HUD confirm HUD's understanding that the HAP contract remains in force after a refinancing.

To remedy this newly discovered problem, HUD proposes to allow owners of refinanced projects, both past and future, three choices, one of which is opting-out of the Section 8 program. As if we did not already face a huge challenge to preserving extremely affordable rental housing, with the stroke of a pen, HUD has put at-risk the homes of 100,000 seniors and families with children, added hundreds of owners to the numbers already considering opting-out of the Section 8 program and raised questions about the financial security of bonds issued to finance Section 8 developments.

This HUD opinion is a fiasco. It raises three questions about HUD's stewardship of precious affordable housing resources. The first question is what is HUD's policy on preservation? States are investing hundreds of millions of dollars and thousands of person hours in very complicated transactions to preserve, not just State-financed housing, but housing financed by the Federal Government, HUD, and USDA rural development.

In Minnesota alone, the State legislature appropriated $60 million in State general funds in addition to our other resources, and we have locked in 6,000 units of affordable housing, 80 percent of which were financed originally by the Federal Government, not the State. Many of us at the local level, HFA's, cities, tenants, owners, and advocates feel that we are going it alone in caring about preserving this critical housing.

Some in Minnesota have questioned why we would put State resources into preserving HUD-assisted housing when HUD is not. How long is this sustainable without HUD as a genuine partner?

The second question is what kind of business partner is HUD? How should Standard & Poor's or Moody's rate bonds in the future that are dependent on a contract with HUD. Should for-profit or

nonprofit owners participate with HUD in the future in programs or transactions that require that they take any risk?

The Minnesota Housing Finance Agency, taking its very cautious approach, got prior approval from HUD for every refinancing we did. How can HFA's or anyone rely on anything HUD says if they can disavow their words and actions decades after the fact?

The third question is what does this demonstrate about HUD's administration of housing programs? HUD, in essence, is saying that for at least two decades, HUD's staff, under both Republican and Democratic Administrations, improperly paid out billions of dollars of rent subsidies, that no one asked whether it was legal and that HUD just noticed it.

Depending on what you think of the OGC's opinion, HUD was either wrong for 27 years or they are wrong now. Neither scenario inspires confidence. While I am not here to debate the legal questions involved in that, suffice it to say that NCSHA firmly believes that this decision was not compelled by the language and that the opinion might have been rendered differently if HUD had been guided by a strong policy commitment to preserving Federally-assisted housing.

In conclusion, HUD has seriously exacerbated an already serious problem. The opinion of the OGC is plain wrong. HUD should reconsider the opinion and reverse it. Failing that, we are exploring our options, including working with HUD, and with you, Mr. Chairman, Senator Sarbanes, and others to devise legislation that will fix this problem.

Thank you very much for your concern for preservation and for your close attention to this specific matter.

Senator REED. Thank you very much, Ms. Hadley.

Mr. Slemmer, welcome.

STATEMENT OF THOMAS W. SLEMMER
PRESIDENT, NATIONAL CHURCH RESIDENCES
COLUMBUS, OHIO
ON BEHALF OF THE
AMERICAN ASSOCIATION OF HOMES AND SERVICES FOR THE AGING

Mr. SLEMMER. Thank you, Mr. Chairman and Members of the Subcommittee. I am Tom Slemmer, President of National Church Residences. I am also Chairing the Preservation Task Force of the American Association of Homes and Services for the Aging. Just to refresh your memory, we have 5,600 members, not-for-profit members, who are operating about 300,000 units of affordable housing under some form of Federal subsidy or sponsorship, about 70 percent faith-based. I am also one of the founding members of the Stewards for Affordable Housing for the Future. Just to give you the not-for-profit perspective on this, we represent about eight large not-for-profits around the country, about 65,000 units of housing that wants to send the message that not-for-profits have the capacity and the willingness to participate in this issue of preserving affordable housing.

I want to focus my comments a little bit on the not-for-profit senior housing perspective. Our testimony speaks to many aspects of preservation, but one of the things that we want to say is that we

are really alarmed about what is happening to the loss of affordable senior housing.

We fear that we are going to lose every single unit that is in a good market area—I mean that—especially if you look at the 236 portfolio. The market forces are moving so fast that it is just almost impossible, without some kind of leadership, to really turn around the properties that are located in prime areas. We are seeing it on the West Coast and the East Coast, but other areas, also.

I thought I would just mention quickly that vouchers do not work for seniors, and we need to really think about that. The project-based Section 8 is really important for senior housing because it is not just addressing the affordable housing situation. It is really serving a more complex array of issues, and it is really a great success story of this Congress—the development and the operation of affordable senior housing.

Vouchers may work, but they certainly encourage scatter sites. Senior housing really concentrates on density, and with that density we are able to provide more services, we are able to get more community involvement, we are able to foster more supportive housing systems, reduce isolation on and on. Senior affordable housing is a bargain for this country, and people are starting to recognize it is part of this long-term care strategy that we are going to have to develop here as the baby-boomers, like myself, become seniors here in the next 10 years.

Mission-driven not-for-profits have a will and a desire to participate in this affordable housing preservation, and we are really alarmed. You have already recognized the need. We find in our membership there are eight people on the waiting list for every Section 202 housing facility in this country. Somebody from New York just told us today they have 10 units available this year, 1,500 on the waiting list. Lots of need that is well-documented.

We want to focus our recommendations on three issues. We think we need leadership from HUD, we need incentives for sellers to participate in a preservation process, and we need a few tools to make this happen. I say that in that order because it really is about leadership. HUD has many of the tools available right now to help us preserve this kind of housing.

Owners must have an incentive to get them to participate in what is clearly a longer process of putting together the financing package for a preservation plan. There are some tools out there that we need to talk to you about as it relates to how to help us with this.

Vouchers, for example, are a problem. The enhanced voucher program, we think you should rename that and call it a transition voucher, because what it is doing, in many cases, is helping owners transition their property to a market-rate product. We think you should come up with a preservation voucher, a voucher that allows a preservation entity, a not-for-profit preservation entity, to participate in this voucher pool when they are actually trying to preserve this housing.

In just a few moments, I want to tell you about a project in Kansas that we preserved, and I have copies of this I will share with you later, but a beautiful 50-unit property, Manhattan, Kansas, a town of 50,000, and it is a success story that I think if we could

figure out the components that made that successful, we might be able to find a solution in the future.

We had an owner opting-out. He announced his opt-out. The community and the residents were involved. They were concerned about this. We received the national HUD office's and the local HUD office's participation in a preservation plan. We were able to get the State Housing Finance Agency to score us high on a preservation tax credit allocation. The Federal Home Loan Bank Board became involved, and we put together a package that preserved this project, in perpetuity, for affordable senior housing—great location, great group of anxious seniors.

And it really required the leadership to pull all of this off, and that is the kind of leadership we think it is going to take to solve this problem with preservation. We have to have a focal point nationally that says, this is a problem. We have to figure out how to expedite the tools that we have available to get us to be able to move faster, to keep up with market forces, and we have to coordinate with State Housing Finance Agencies to make sure that they are on board with preservation tax credits, and we have to get the private grants involved to provide incentives.

We see properties like this that do not have that kind of support come on the marketplace for sale and are gone in a matter of a few months. We are working on one right now in Cleveland, where the owner decided to opt-out. It is a Section 236 elderly property. The opt-out, we really could not slow it down because of enhanced vouchers, there was no community to preserve that housing, and we were not able to slow it down because, with enhanced vouchers, the owners are able oftentimes to get extra cashflow into their property, and they can change their property from an affordable product to a market-rate product without any loss of revenue. We were almost facilitating that change.

We are working on a lot of preservation projects. Virtually every one requires HUD leadership. In many cases, we are getting outstanding leadership at the HUD local level. I would just encourage you to think about—leadership is really important here. We have a lot of tools available, a lot of people around this country that are interested in preservation. We have to figure out a way, like the Millennium Housing Commission suggestion, with some kind of preservation tax credit that gives relief to the owners for hanging in there in the preservation process, and we have to work on a few more tools to put in the hands of qualified preservation entities so we can participate in the preservation.

But there are not-for-profits with the will and the capacity out there to really make a difference in this problem.

Senator REED. Thank you very much, Mr. Slemmer.

Ms. Sanchez.

STATEMENT OF LOUISE SANCHEZ
PRESIDENT, NATIONAL ALLIANCE OF HUD TENANTS
NEW YORK, NEW YORK

Ms. SANCHEZ. Thank you, Senator Reed, for your leadership in calling this hearing and for the invitation to testify before you.

Founded in 1991, the National Alliance of HUD Tenants is the Nation's only membership organization representing the 2.1 million families who live in privately-owned, HUD-assisted housing.

This past weekend, NAHT released a report in several cities showing that the United States has lost more than 250,000 units of affordable housing since 1996 when Congress restored owners' ability to prepay their 40-year HUD-subsidized mortgages without major restrictions. Of this amount, close to 200,000 units of HUD-subsidized housing were lost due to owner decisions to prepay or to opt-out of expiring project-based Section 8 contracts as of August 2001. The remaining units consist of public housing units lost through the HOPE VI demolitions. We are submitted a copy of this report,* by the way, with my testimony today.

Many observers thought that the problem of the loss of housing was solved when the Congress and HUD adopted the Mark-Up-to-Market Program in 1999. However, our report shows that, despite this program, the average loss of housing nationally has remained roughly the same as before its adoption. About 41,000 units continue to be lost each year. We clearly need to do more to preserve the Nation's affordable housing stock.

Some areas have been particularly hard hit. By August 2001, California and Texas alone had lost over 65,000 units of privately-owned affordable housing, nearly a third of the national total. Some 14 States have seen an increase in the rate of either the opt-outs or prepayments by more than 300 percent since early 1999.

Most startling of all, however, is the new data we are releasing today regarding New York City, which is where I come from. We have already lost more than 8,000 units in New York City alone, and owners of another 5,767 units in the 11 Mitchell-Lama developments have filed notices of intent to prepay. In addition, four co-ops housing more than 25,000 families, including the 15,000-unit Co-op City development, are planning to privatize and prepay their mortgage in the next year. All told, we have lost or expect to lose some 40,000 units of affordable housing in New York City by the end of next year.

In the wake of the trauma inflicted on New York City in the past year, the imminent loss of 40,000 affordable housing units is a crisis which we can neither bear nor ignore.

Homeland security begins with a home. Action by the Congress is urgently needed to give us the tools to preserve these affordable units. It is now clear that voluntary incentives are insufficient to save affordable housing. NAHT believes that Congress should establish a national regulatory framework, like the Title VI Preservation Program, repealed by Congress in 1996, to limit owners' ability to opt-out and prepay.

Ironically, in buildings where HUD is executing 5- to 20-year Mark-Up-to-Market contracts, the cost of additional Section 8 subsidies is approaching the cost of the Title VI Preservation Program, but with none of the benefits in terms of mandatory repairs, permanent affordability, and transfers to nonprofit purchases. Worse, the 5-year extensions in most Mark-Up-to-Market buildings leave residents and HUD at continued risk.

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*Held in Committee files.

Deregulation is a strategy that has failed in the energy, telecommunications, banking, and airline industries in the United States and in countries around the globe. Now the evidence is in: Deregulation is a failure in the subsidized housing industry as well. Congress should act now to restore regulations to save our homes.

Besides the Congress, HUD needs to do more to save affordable housing. Instead, HUD's policies have added to the loss of housing rather than its preservation. For example, HUD's policy of dumping properties it owns or controls on the open market with vouchers for tenants and toothless use restrictions has resulted in the loss of 26,000 apartments by March 2000, a significant portion of the 86,402 project-based Section 8 opt-out units lost between 1996 and 2001.

The NAHT has challenged a variety of discretionary HUD policies which have added to the needless loss of housing. Our written testimony goes more into this in detail. In the interest of time, we will limit our remarks here to suggesting the three key questions for which we would like some answers today with the Subcommittee's help.

Will HUD adopt a comprehensive policy to maximize preservation of at-risk housing in areas where HUD has discretion to do so?

Will HUD enforce—enforce—the law and sanction owners where owners fail to accept enhanced vouchers as required by Congress or comply with Federal or State notice requirements as required by HUD's own Section 8 policy?

And will the Commissioner and his staff meet with representatives of NAHT, the National Housing Law Project, and key Subcommittee staff to discuss and resolve the specific cases we have raised in our testimony today?

Since NAHT was founded in 1991, we have sought to establish a partnership with HUD whereby the tenants, the people with the strongest stake in the successful operation of HUD housing, serve as the unpaid volunteer's "eyes and ears" of HUD in overseeing owners and managers of our buildings. Congress has supported this vision by providing up to $10 million annually through Section 514 of the MAHRAA to promote tenant and community petition in Section 8.

I will conclude with this. Most devastating to tenants has been HUD's continued failure to restart the VISTA Volunteers Project in HUD housing. Funded by a HUD interagency agreement with the Corporation for National and Community Service since 1995, this successful project has helped to empower tens of thousands of residents in HUD multifamily housing to participate in saving and improving their homes. The program costs HUD very little money and leveraged an equal amount of resources from CNCS to place an average of 50 VISTA's each year with 30 local groups. CNCS has pledged its support for a 3-year extension of the program if HUD is willing. This program has been frozen since November 2001, when HUD failed to honor its contract with CNCS, even though in March, Secretary Martinez and Commissioner Weicher told Congress that the VISTA project would be restarted immediately and that the $600,000 owed to CNCS by HUD was being processed. He said he was going to do it as soon as he left here and went to his

office. I can only assume he never found his way to the office because the bill was never paid.

The other part of the problem is that much to HUD's embarrassment, in the ongoing Section 514 fiasco, it could have been avoided had the new leadership team communicated with NAHT. In the 25 years NAHT and its leaders have been dealing with HUD, this is by far the least responsible and accessible leadership at the Agency we have ever seen. Far from being treated as partners, this Administration treats tenants and the people who work with us as if we were the enemy. We ask the Subcommittee's help in helping us reestablish the kind of dialogue and partnership through regular meetings with the Secretary and the Commissioner, which we have enjoyed with several previous Administrations.

We ask Congress to adopt legislation to save our homes. We urge that the Subcommittee support S. 1365, the preservation matching grant. We urge Congress to restore regulatory measures to prevent displacement and preserve affordable housing, like the former Title VI Preservation Program. And, finally, if I can turn the page, it is not too early for Congressional leaders to develop a long-term legislative strategy to save our homes.

I refer you to the written report, and, again, let me thank you for allowing us to testify.

Senator REED. Thank you, Ms. Sanchez.

Thank you all for your testimony. I have questions for all the panelists, but let me begin with Ms. Hadley.

You listened to the exchange about the HAP program, and just for some further context, over the course of 20 years in Minnesota your lawyers, who looked at these refinancings, and the developers who came in, did they ever raise the question of the applicability of the Section 8 provisions?

Ms. HADLEY. Mr. Chairman, the issue of what happens upon a refinancing was, in fact, addressed by HUD's staff, both program staff and attorneys working for HUD. It came up in a variety of different ways, and we have submitted letters to HUD and other documents that demonstrate that. So, we think, in fact, HUD's staff was doing their job for the last 20 years. They were considering the question of what happens upon a refinancing with the HAP contract, and it was decided correctly all these years.

Senator REED. And, in fact, your perspective also is that the beneficiaries, the owners of these projects understood that too, and there is documentation suggesting—not just practice but documentation suggestion that?

Ms. HADLEY. My understanding is that the owners fully expected that these HAP contracts would continue.

Senator REED. Well, we would be interested in some of those documents. Staff, I am sure, will contact you. But thank you so much. I still remain amazed at this startling reinterpretation.

Mr. Grow, your testimony talked about the hostility toward preservation, and I think, Mr. Slemmer, essentially the same thing. Why don't you comment on HUD's policy with respect to foreclosure and to the extent that leads you to believe that there is this real hostility? And your comments, too, Mr. Slemmer, about the 202 program would be helpful.

Mr. Grow.

Mr. GROW. Well, I feel like I saw this movie a long time ago. Congress wrestled with this issue in the early 1980's, held a lot of hearings, issued reports, enacted legislation in 1988 requiring HUD to preserve multifamily properties that were being sold at foreclosure or were HUD-owned.

A few years later, when the Congress—or HUD did not request adequate budget authority to run the program, HUD came—the Clinton Administration came to Congress in 1994 and said, we need some relief from this, we cannot manage all these properties that are in trouble, so let's devise some more "flexible" authority. That is a bad term because that was used subsequently to justify deregulation. But Congress worked very hard with the Administration in 1993 and 1994 to come up with the Multifamily Property Disposition Reform Act.

Well, before the ink was even dry on that statute, which establishes public policy criteria governing HUD's foreclosure and property disposition activities, as well as its mortgage sale activities, HUD was back in here in 1995, requesting that Congress give it blanket authority to do whatever it wants. And Congress did that.

So, I cannot imagine that an agency that was committed to preserving affordable housing would not be able to work within the statutory framework that Congress had already crafted.

There have been repeated instances—it was interesting listening to the explanation of Brick Towers and the exchange between the Commissioner and Senator Corzine. Brick Towers was sold not for preservation but to the Newark Housing Authority for demolition, despite the city council's having passed an ordinance prohibiting demolition.

So to hear them say that, well, the State or the local government has the right of first refusal is really disingenuous because that right of first refusal was exercised, and they did not get their act together, and that contract of sale expired numerous times. HUD could have easily said the deal is off, we have to sit down and work something else out. And they never did that.

Senator REED. Thank you, Mr. Grow.

Mr. Slemmer, you have done, as you indicated in your testimony, a great deal of work with elderly housing, Section 202 programs, and your perspective, too, about these foreclosure issues. I think it was a point Mr. Grow established that this is not a recent problem. This goes into the Clinton Administration, too. But whether or not there is a more difficult situation today or this is just a continuation of the insensitivity that has been for years.

Mr. SLEMMER. That is a good question. We have documented in our testimony three foreclosures of Section 202 elderly properties that really are alarming to us. "Hostility" is not a good word for it, I would suggest. These properties got caught up in property disposition, and it is just a lack of awareness that they should stop and do something about it.

The concern we have had primarily is not that you won't find elderly housing every once in a while get into problems and then end up in property disposition. But the lack of interest in bringing in someone else, another not-for-profit to be able to step in and operate that housing.

In Detroit, for example, we had two large not-for-profit organizations that were willing to step up, and in Upstate New York, the one we document is in Alfred, New York, we had our organization willing to step in, and just the inability to effect the process once the gears got rolling.

I would say as it relates to preservation, "hostility" is not a good word. In our experience, it is more of a lack of awareness of what the loss of this housing does to the community. And when you can convince the HUD office of that, we find oftentimes there is more leadership at the local level than you could get at the national level in terms of people saying, yes, let's figure out what we can do to save the homes of these people.

Senator REED. Is this a lack of resources at the local level or a lack of a policy directive from Washington saying get interested in this? And I think you have very clearly stated it is not, you know, do not do this at all, but it is just not making it a priority?

Mr. SLEMMER. Typically a HUD transaction, if you have tax-exempt bonds or you have tax credits involved, it is a year to a year and a half process. And than getting everyone, HUD and the other agencies, to understand that preservation requires speed is very difficult.

We find, for example, that oftentimes the tax credit cycle will not coincide at all with the property that is offered for sale. Therefore, convincing the owner to hang in there while you go through this process is very, very difficult. But I think leadership is the key. Focusing all the resources we have on this effort would make a difference.

Senator REED. Thank you.

Ms. Sanchez, your testimony also suggests—and the question I raised with Secretary Weicher—about the failure to give proper notice. Is that a problem you see increasing?

Ms. SANCHEZ. Yes, it is. And, in particular, I think there were five States that I may have cited—California—I need to put my glasses on. California, Minnesota, Missouri, New York, and Pennsylvania in a sense immediately come to mind.

But the whole question of notice becomes paramount because if tenants do not get proper notice, in the sense of, first of all, the time period, there is so much work that has to be done in terms of still trying to preserve their housing, that they will not have time to do, and that is because of the absolute refusal of HUD to do any homework on opt-out applications or prepayment applications. They routinely approve them. They do not check into things that they should be checking into—land-use options.

They approved a buy-out in Manhattan 4 years ago for a development on 23rd Street. That buy-out has not taken place yet because the tenants went in and litigated on the land use. There was a covenant with the Board of Estimates that said that no matter who owns the property, the apartments have to remain affordable for another 75 years.

Why HUD doesn't do this, why the burden falls on tenants to go check this out—they need the time to check it, they need the resources, the money which goes into the OTAG funds and the ITAG funds which are all blocked up again right now. It is a losing game if they, in truth, are out to preserve affordable housing.

I fail to understand why they do not do a little bit of homework but shove it all on the backs of tenants to do all the research for themselves.

Senator REED. Thank you very much, Ms. Sanchez.

I want to thank all of the panel for your excellent testimony, your comments, and your insights, and it seems apparent today that leadership is necessary by the Congress, the President, and the Administration at HUD to once again focus attention on preserving affordable housing. And without that leadership, without that attention, we will see a continuing erosion of affordable housing. It doesn't help when some inexplicable decisions are rendered by the Counsel's Office which accelerates that erosion.

We are all committed here, and I think that is a commitment shared not only by this panelist but also by Secretary Weicher, by Secretary Martinez, and by the President to ensure that people have a chance to live in decent housing. But the rhetoric has to be matched with action and leadership and commitment. I hope we can do that.

I would ask if there are additional questions, or material, or responses, if we ask you questions, please to submit them by October 16. In fact, let me get this right. You might receive questions from my colleagues prior to October 16. Please within 10 days respond. And if you have anything you would like to send in, that is okay.

Thank you very much. The hearing is adjourned.

[Whereupon, at 4:25 p.m., the hearing was adjourned.]

[Prepared statements, response to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF JOHN C. WEICHER

ASSISTANT SECRETARY FOR HOUSING AND FEDERAL HOUSING COMMISSIONER
U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

OCTOBER 9, 2002

Chairman Reed, Ranking Member Allard, and distinguished Members of the Subcommittee, thank you for inviting me to testify on the subject of affordable housing preservation.

You have asked me to discuss specifically several matters that concern the preservation of the existing stock of affordable housing. I am happy to do that, but before doing so, I would like to describe several of the Department's initiatives to increase the available inventory of affordable housing.

In the fiscal year just completed, the Federal Housing Administration's basic multifamily housing insurance program, Section 221(d)(4), experienced a very substantial increase in activity. Overall, FHA made commitments for 198 new construction or substantially rehabilitated projects, with over 38,000 units and totaling $2.8 billion worth of mortgage loans. That total dollar figure is easily the biggest number for the program in the last 10 years, and could well be a record. It is almost double our activity in fiscal year 2001. Last year, FHA made commitments for 139 projects, with over 21,000 units, totaling $1.5 billion. That amounts to a 42 percent increase in the number of projects, a 79 percent increase in apartment units, and an 85 percent increase in the dollar value of commitments.

One major reason for this dramatic increase is that, in fiscal year 2002, HUD was able to operate Section 221(d)(4) on a self-sustaining basis. By raising the mortgage insurance premium to 80 basis points, we were able to end the program's dependence on credit subsidy and terminate the need for appropriations. There is no longer any need for the industry to be concerned about program delays and stoppages because of credit subsidy issues. During the last 8 years—from 1994 through 2001—FHA's credit subsidy programs had to discontinue operations three times.

I know that many people in the industry were concerned that raising the premium would cripple the program. Clearly, that did not happen.

Having put Section 221(d)(4) on a self-sustaining basis, FHA is now in a position to reduce the insurance premium to 57 basis points, which will make the financing of new or rehabilitated apartments more affordable. The reduction is a result of a comprehensive review of the credit subsidy calculations for all FHA's multifamily programs, the first such analysis in a decade. You may recall from my confirmation hearing that I made a commitment to conduct this study. FHA began work on the study in June of last year, and we completed it in time for the new credit subsidy calculations and premiums to be included in the President's Budget for fiscal year 2003 and to go into effect at the beginning of this fiscal year. We have lowered the premium on several self-sustaining programs, and lowered the credit subsidy rate on almost all of those that still require credit subsidy. The proposed notice for the premium reduction was published in the *Federal Register* for comment in August with comments due by September 30. We expect the final notice to be published within a matter of days and FHA will permit Section 221(d)(4) commitments that have not closed to be reprocessed at the 57 basis point premium.

There are other reasons for the sharp rise in commitments. Shortly after he came to HUD, Secretary Martinez announced his support for a 25 percent increase in the statutory per unit limits for the FHA's multifamily mortgage insurance programs. This was the first increase since 1992. The increase helps to make the FHA programs more feasible in high-cost areas where the programs had not been used for several years. Philadelphia, for instance, has seen its first FHA-insured multifamily projects in more than 5 years. Mortgage insurance applications have been submitted to finance developments in Washington, DC, Baltimore, St. Louis, and suburban Minneapolis that would not have been submitted without the increase in the limits.

The Multifamily Accelerated Processing (MAP) Program is another contributing factor. Having now completed 2 full years of this program, we have done more to standardize the process, and we have demonstrated to the development industry that FHA's field staff can and will provide an expedited review of the mortgage insurance application packages.

I also want to briefly touch upon some of this Administration's fiscal year 2003 budget proposals that will increase access to or add to the current inventory of affordable housing.

The Administration's Budget for this fiscal year includes an additional $200 million in funding for 34,000 rental housing vouchers, in addition to the 1.74 million vouchers currently being utilized by low-income families. The Senate Appropriations Committee only provided funding for 17,000 new vouchers. The Administration

strongly urges Congress to fully fund our request, either by the full Senate or in conference.

Although the national vacancy rate is close to an all-time high—8.5 percent in the second quarter this year—there are still areas of the country with a low-vacancy rate. To address this problem, the Administration also supports the development of affordable housing through programs such as the Low-Income Housing Tax Credit, which supports about 100,000 new or rehabilitated rental units each year. Two years ago, Congress enacted a 40 percent increase in the volume limits for the LIHTC, and caps for tax-exempt housing bond financing were also raised last year. States can direct these resources to the local markets where supply is constrained or rents are highest.

In addition, the Administration has asked for increased funding this fiscal year for the HOME block grant program. At the proposed $1.8 billion funding level, HOME will produce 23,000 new affordable units and a similar number of rehabilitated units. Provision of these units will be made through decisions by local governments concerning their own affordable housing needs. Families with extremely low incomes will occupy over one-half of these units. By law, Section 8 Voucher holders have access to all units developed with HOME and/or LIHTC support.

HUD's Section 202 elderly housing, Section 811 Disabled Housing and Housing Opportunities for Persons with AIDS programs also produce thousands of new units a year for special populations.

I would also like to report progress on one of the first initiatives I undertook after becoming FHA Commissioner, and that was to take a look at the large number of projects in the development pipeline in the Section 202 and Section 811 programs. A report prepared for GAO had indicated that there were over 100 Section 202 projects from the years 1992 to 1997 that had not reached initial closing. I directed our Office of Multifamily Housing to determine the status of these projects. We learned that the pipeline data was badly out of date. Of the 100 projects listed as being in the pipeline, 25 had cancelled—some years ago—and 18 had already closed. I then directed our staff to bring as many of these old project commitments as possible to closing, and I am pleased to report that we closed 30 of them.

At the end of fiscal year 2002, the combined total of Section 202 and Section 811 projects funded between 1992 and 1997 that had not reached initial closing is now down to 26. That number represents only 1.3 percent of 2,058 projects funded during that 6-year period. This fiscal year, I expect those 26 will be closed or cancelled, unless they are in litigation.

We will continue to try and make improvements to ensure the timely development of affordable housing under these programs and are working with our field staff to help accomplish this. We recently completed two training sessions for our field staff, the first such training in 11 years. In addition, we changed the awards process so that it does not reward sponsors that previously have been unable to demonstrate that they can develop affordable housing in a timely manner.

I would now like to address some of the issues this Subcommittee has raised concerning the preservation of the existing stock of affordable housing.

Preservation of the Existing Section 8 and Section 202 Affordable Housing Stock

The Department is committed to preserving the existing stock of affordable rental housing. Over the last few years, the Congress through legislation has provided for financial tools to provide incentives and assist project owners to preserve the affordable housing stock. Working with Congress, the Department has been successful in a number of areas in its efforts to preserve the affordable housing stock as well provide incentives to the owners.

The Department implemented Mark-to-Market and Mark-Up-to-Market to provide opportunities for owners to make capital improvements and the necessary repairs to ensure the units are decent, safe, and sanitary for the residents and to ensure the units remain affordable.

Since the inception of the Mark-to-Market Program, HUD's Office of Multifamily Housing Assistance Restructuring (OMHAR) has successfully closed debt restructurings on 571 properties. These properties include over 46,000 units and are now subject to 30-year Use Agreements. They were provided with over $62 million in escrows to repair properties, and an infusion of approximately $40 million in immediate Reserve for Replacement deposits, increasing the long-term physical stability of the properties. In addition, OHMAR has processed Section 8 contract renewals and reduced rents on over 120,000 units, resulting in annual Section 8 savings of over $105 million.

The Mark-Up-to-Market Program, created in fiscal year 1999, has been similarly successful. In its first 4 years, through fiscal year 2002, 632 Section 8 contracts have

been renewed and 58,000 affordable housing units were preserved under this program. To be eligible for the Mark-Up-to-Market, a property must: (1) Not have a low- and moderate-income use restriction that cannot be eliminated by the unilateral action of the owner; (2) be decent, safe, and sanitary; (3) not be owned by a nonprofit entity; (4) not be a Section 8 Moderate Rehabilitation Project; and (5) have rents exceeding 100 percent of fair market rents.

Additionally, the Department uses its statutory authority to enter into multiple-year Section 8 contracts for those owners choosing the Mark-Up-to-Market rent increase option. Owners must enter into a contract at a minimum of 5 years, but not to exceed 20 years. Payments under the contracts are subject to the availability of appropriations. To limit the possible cost to the Government for implementing the MU2M option, the Department capped the rent increase at the comparable market rent or 150 percent of fair market rents, whichever is lower.

The Department also recognizes the important contribution that has been made by nonprofit owners in the development and the preservation of affordable housing. This is particularly true for those nonprofit sponsors who have developed Section 202 affordable housing for the elderly and persons with disabilities. Many of the older Section 202 projects have Section 8 rental assistance. The owners of these projects are eligible to apply for an increase in their rents to cover the cost of capital repairs. The program requirements and process for obtaining the rental increase is described in Chapter 15 of the Section 8 Contract Renewal Guide. From fiscal year 1999 through fiscal year 2002, 1,092 Section 8 contracts in the Section 202 program have been renewed, with more than 80,000 affordable elderly and disabled housing units preserved.

For all Section 8 project-based programs combined, during the last 4 fiscal years, a total of 10,695 Section 8 contracts were renewed and over 778,000 affordable housing units have been preserved.

HUD's Interpretation of Section 8 Contractual Provisions for State Finance Agency-Financed Multifamily Projects

The Department's Office of General Counsel recently issued a legal opinion regarding the contractual provisions governing the term of a Section 8 Housing Assistance Payment Contract (HAP) between a State Housing Finance Agency and an owner for a State Housing Finance Agency-financed project executed prior to 1980. It is HUD's position that this is neither a new policy nor a reinterpretation. The Section 8 contracts in question provide that the term of the contract terminates "on the date of the last payment of principal due on the permanent financing." It is my understanding that up until the recent OGC opinion, Housing Finance Agencies have interpreted the HAP contract language to mean that new financing is included as "permanent financing," and that the contract does not terminate when an owner refinances the original mortgage.

The Department has identified approximately 1,400 Section 8 HAP contracts at most that potentially could be impacted by this recent OGC opinion. This maximum number could be further reduced by the dozen or so States that have strong prepayment restrictions. In an effort to lessen the impact of this opinion on the existing assisted tenancies, minimize the loss of affordable housing units, and to assure the availability of continued rental assistance for project residents, HUD has proposed to the State Housing Finance Agencies two alternatives for the affected project owners: (1) The owner may elect to extend the maximum term of the HAP contract from the date of the prepayment to terminate at the originally scheduled maturity date of the permanent financing. (2) The owner may elect to renew the project-based Section 8 contract in accordance with the Multifamily Assisted Housing Reform and Affordability Act (MAHRAA).

However, an affected owner could choose neither option and exercise the right to opt-out of the Section 8 contract. In this case, the owner must provide HUD and the tenants with the proper 1-year notice of HAP contract termination.

We recognize the concerns of project owners, State agencies, and Members of Congress about the potential consequences for the affordable housing stock, and we have been discussing the situation and possible options with the Council of State Housing Finance Agencies, among others.

Status of Regulations that Will Allow Nonprofit Organizations to Create For-Profit Limited Partnerships for the Section 202 Program

The original law that allowed for-profit participation in the Section 202 program was included in the American Homeownership and Economic Opportunity Act of 2000. Included in the same Act, was a provision related to the refinancing of existing Section 202 projects. On August 23, 2002, the Department issued Notice H2002–16 to implement this provision. Since then, my office has focused its efforts on the

rulemaking associated with the provision regarding for-profit participation in the Section 202 program. We are working diligently on the required regulation and expect to submit it to OMB for review in the near future. We know that the nonprofit organizations are eager to use the capital advance to leverage additional funds to develop more additional affordable housing or services for the elderly. HUD funded eight Section 202 projects in fiscal year 2001, where the sponsors indicated that they anticipated developing a mixed-finance project.

HUD's Enforcement of Regulations When Owners Opt-Out of Section 8 Contracts

We have been pleased to work with the Members of this Subcommittee to ensure that owners with developments that have project-based Section 8 assistance provide proper notice when opting-out of the Section 8 program. It was never the intent of the Department to reward owners who do not comply with the required Federal notice requirements. The forthcoming revisions to the Section 8 Contract Renewal Guide will clarify this point, and will be available within the next few months. We have worked with our Offices of General Counsel and Public and Indian Housing to develop a consistent policy that does not reward owners yet protects the tenants at the projects where the owner chooses to opt-out.

Any owner who fails to provide proper 1-year opt-out notification must permit the tenants to remain in their units without increasing their portion of the rent for whatever period of time is necessary to meet all of the notification requirements. Eligible families residing in the property will be issued vouchers when the contract expires. The family may use the voucher to remain in their current unit or elect to use the voucher to move to another property. Should the family elect to remain in their current unit, the voucher housing assistance payments contract does not commence until the full 1-year notice requirement has been met. The effect of this action is that the owner will not receive any voucher assistance payments until proper notice has been provided to the tenants.

In instances where project owners need additional time to meet the 1-year notice requirement, they are encouraged to enter into a short-term contract renewal with a term long enough to ensure that the tenants receive a full 1-year notice of contract expiration. Otherwise, the owner will only receive the tenant portion of the rent the families were paying under the expired contract until the full 1-year notice period has been met.

Status of the Utilization of Interest Reduction Payments Funds to Rehabilitate Existing Affordable Housing

The Department will continue to consider the implementation of Section 236(s) depending on the availability of future year Section 236 recaptures. Questions regarding the availability of funds derived from old contract authority converted to budget authority were not resolved until the spring of 2002.

As Members know, the Emergency Supplemental Appropriations Act included a $300 million rescission of recaptured IRP funds from mortgages insured by Section 236 that have been prepaid. At this time, it does not appear that there are adequate funds beyond the rescission to implement a program.

Estimates of future prepayments which provide the recaptured funds available for rehabilitation are uncertain. Two initiatives by the Department that help to preserve the affordable stock have reduced the amount of future IRP funds available for recapture. HUD allows Section 236 owners to decouple the IRP from the mortgage at prepayment in return for extended affordability restrictions. Those IRP funds are not available for recapture.

In addition, Section 236 owners with Section 8 subsidies may apply to have their Section 8 rents Marked-Up-to-Market. Approximately $40 million in IRP funds have been used to capitalize project reserves for replacement for projects that have been Marked-to-Market by OMHAR.

This concludes my statement, Mr. Chairman. Thank you for the opportunity to appear before this Subcommittee.

PREPARED STATEMENT OF JAMES R. GROW

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OCTOBER 9, 2002

Mr. Chairman and Members of the Subcommittee. Thank you for this invitation to testify today on the important issue of preserving the existing privately-owned

affordable housing stock currently supported with public funds under a variety of Federal housing insurance, subsidy, and assistance programs.

The National Housing Law Project is a charitable nonprofit organization providing legal and technical support for housing advocates, tenant leaders, and public officials nationwide on the housing issues confronting Americans with incomes at or near the poverty level. Our support role has included legal research, advice, and co-counsel regarding litigation matters, legislative, and administrative advocacy with Congress and State and local governments, publication of our *Housing Law Bulletin* and housing law manuals, and training and technical assistance. The views presented here reflect the work of the Project over more than 30 years since its creation in 1968. Working with local housing advocates, dealing with the day-to-day problems and opportunities presented by implementation of Federal housing laws and programs, has developed the views we express today.

This privately-owned, Federally-supported, affordable housing stock totals more than 1.5 million units in more than 10,000 properties located throughout the urban, suburban, and rural areas of our Nation, providing affordable housing to more than 3 million seniors, people with disabilities, and families with low and very-low incomes. These units, regulated by HUD and the USDA's Rural Housing Services under a variety of mortgage loan and rental assistance programs, represent more than one-third of our country's deeply subsidized affordable housing inventory intended to meet the critical and growing needs of lower-income Americans for decent affordable housing. The vast majority of residents who call these units home have very-low annual incomes, many below $10,000.

One of the major design weaknesses of these programs is that the affordability restrictions accompanying the Federal financing or the subsidy itself are time-limited and expire at some point. Without further Federal budget authority *and* a commitment or requirement that the owner continue to provide affordable housing, the stock faces a risk of conversion to market-rate use.

Our statement first focuses on the recent legal and policy background of the preservation issue, before moving to several specific areas of concern that require Congressional oversight or legislation.

Recent Historical Background

Over the last decade, Federal budget priorities have driven substantial changes in Federal preservation policy. Prior to 1994, virtually all units were protected through a variety of Federally-funded statutory policies and programs, such as the preservation program for units facing prepayment risks and the property disposition program for troubled developments. In 1994, Congress relaxed the preservation requirements governing HUD's multifamily foreclosure and disposition practices. "Multifamily Housing Property Disposition Reform Act of 1994," Pub. L. No. 103–233, 108 Stat. 342 (1994), *primarily codified* at 12 U.S.C.A. § 1701z–11 (West 2001). In 1995, a new Congress went even further in an emergency supplemental appropriations law, arguably granting HUD broad and standardless discretion over these issues. Pub. L. No. 104–19, 109 Stat. 194, 233 (1995). Simultaneously, HUD promoted its "Reinvention Blueprint," a radical proposal to substitute vouchers for all project-based assistance, including public housing. While not endorsing HUD's proposal, in 1996, Congress reduced funding for the Title VI preservation program for properties with HUD-subsidized mortgages, permitting owners to prepay their mortgages and terminate prior Federal affordability and occupancy restrictions. Congress continued to reduce funding further, while not repealing the program, finally starving the preservation program of any Federal funding in fiscal year 1998. In 1996, Congress also reenacted through the appropriations process the so-called "flexible authority" governing HUD's administration of troubled properties, making it permanent until changed. Pub. L. No. 104–204, § 204, 110 Stat. 2873, 2894 (September 26, 1996) (for fiscal year 1997 and thereafter), *codified at* 12 U.S.C.A. § 1715z–11a(a) (West 2001).

About the same time, Congress faced the question of how to address the problem of expiring Section 8 contracts, some of which were requiring large "above-market" Federal subsidies to support them. Rejecting HUD's voucher plan, in late 1997 Congress passed the "Multifamily Affordable Housing Reform and Affordability Act" (MAHRAA), which provided owners of such properties with the choice to terminate their participation by "opting-out," or to remain in the Section 8 program, generally with new rent levels set at "market" rates. Pub. L. No. 105–65, Title V, 111 Stat. 1343, 1384 (October 27, 1997), *codified at* 42 U.S.C.A. § 1437f (Historical and Statutory Notes, "Multifamily Housing Assistance"). Owners for whom new lower "market rents" would be too low to support debt service and operating expenses could pursue a restructuring plan to reduce their debt service obligations, while usually maintaining their project-based Section 8 contracts, addressing the property's rehabilitation

needs, and committing to a long-term Use Agreement. HUD and other program administrators were also provided with authority to disqualify certain owners from further participation, due to serious prior program violations.

Until mid-1999, HUD did nothing to implement its authority to provide higher Section 8 rent levels at contract expiration to those owners of properties with "below-market" rents. Many owners left the program during this period. In 1999, HUD finally adopted an "emergency initiative" (HUD Notice H 99–15, June 1999) to offer such basic incentives to owners to preserve affordable housing. Recognizing the importance of expanding preservation initiatives, Congress soon after enacted similar "Mark-Up-to-Market" policies into law later that year. Pub. L. No. 106–74, § 531, 113 Stat. 1110 (1999) (extensively revising Section 524 of MAHRAA concerning rent levels HUD can and must offer to various types of properties with expiring Section 8 contracts). While many owners have apparently pursued the "mark up" option, still many others have opted-out of the program.

To its credit, HUD made certain adjustments to the Mark-to-Market restructuring program to provide improved financial incentives for participating owners and purchasers in September 2000.

However, as part of MAHRAA, Congress also established specific authority for Interest Reduction Payments on Section 236 properties with IRP contracts terminated through prepayment or foreclosure be recaptured and used for rehabilitation for other eligible HUD multifamily projects. Pub. L. No. 105–65, § 531, 111 Stat. 1409 (1997). Despite its inclusion in the Administration's fiscal year 2001 and 2002 budgets, HUD has never implemented this grant/loan program, while the available fund grew to $300 million. In July 2002, Congress rescinded these funds in the Supplemental Appropriation to pay for antiterrorism activities. Pub. L. No. 107–206, 116 Stat. 820, 892 (August 2, 2002). Both the fiscal year 2003 Budget and the Senate Appropriations bill project another $100 million being made available in the coming year to preserve and improve properties still at-risk of conversion to market rate.

Congress has also recently expressed concern about the mounting losses of affordable housing, specifically concerning HUD's disposition activities. In March 2000, Senator Bond, then Chair of the HUD–VA–IA Appropriations Subcommittee, issued a statement that was extremely critical of HUD's lax preservation efforts for its troubled projects inventory, and later spearheaded efforts to win passage of provisions explicitly requiring HUD to renew Section 8 contracts at a foreclosure or disposition sale for projects primarily occupied by the elderly and disabled, unless renewals are determined "infeasible." Pub. L. No. 106–377, § 233 (October 27, 2000) (for fiscal year 2001); Pub. L. No. 107–73, § 212 (November 26, 2001) (for fiscal year 2002). Senator Bond has recently introduced a bill which would extend this requirement to all Section 8 properties. S. 2967, 107th Congress 2d Sess., § 203.

Finally, Congress has emphasized the importance of preservation in enacting the "Mark-to-Market Extension Act" last January, extending authority for the restructuring program for another 5 years. Pub. L. No. 107–116, 115 Stat. 2220 (January 10, 2002). One provision requires HUD to develop procedures to ensure that the rents being offered owners to stay in the Section 8 program are comparable to the "enhanced voucher" rents supported by PHA's and Federal subsidies when they "opt-out," § 613. We have heard of no initiative by the Department to address Congress' directive.

Summary of the Current Situation

HUD has demonstrated little capability or initiative to address preservation issues. The Agency has resisted preservation strategies for decades, responding only to statutory mandates that leave it little choice. Left alone, HUD will continue to pursue practices that permit maximum conversion of units to vouchers, reducing its role to only providing annual funding, while shifting all administrative responsibilities to local PHA's.

Federal policy must change. Congress should first request HUD to provide specific information about its activities. Congress should then determine the additional policies and funding resources necessary to establish clearer duties and workable procedures for implementing preservation policies. Broad agency discretion and occasional isolated policies or expressions of concern from Congress are an utter failure.

More funding will be needed to preserve more housing, to purchase properties and ensure their proper rehabilitation. While State and local governments have recently begun to allocate some of their own resources or other funds within their control (e.g., bond financing and tax credits) to meet preservation needs, as well as taking other preservation initiatives such as improved notices and rights of first refusal, they cannot solve this problem on their own. Congress should pursue adoption of legislation (e.g., H.R. 425, S. 1365) to provide "matching grants" to State and local governments that make preservation investments.

Reevaluating the principle of owner choice underlying the current prepayment and opt-out policies should also be reconsidered. Some restrictions that express conscious public policies about which properties should be preserved through additional financial incentives or transfers to tenant-endorsed preservation purchasers will be essential.

The central irony of current Federal preservation policy is that, without preserving housing, the Federal Government is still paying the cost of preserving much of the housing by supporting new "market rents" through the enhanced voucher program. This is true for both units lost through mortgage prepayment and Section 8 opt-outs, at least as long as the tenants choose to remain in place.

Congress' grant of broad discretion to HUD for handling troubled properties and mortgages has not been used creatively to preserve those properties where sufficient tenant and community support has been demonstrated.

Specific Preservation Issues

The following review highlights several areas where Congress should exercise greater oversight of HUD's activities in light of previously expressed statutory preservation policies or expectations, and develop responsive statutory policies. These areas include:

- Troubled Projects Policy
- Prepayment of Properties Requiring HUD Approval
- Revision of Flexible Subsidy Agreements
- Implementation of the Section 531 Rehab Grant Program
- Providing Enhanced Vouchers to Owners Who Violate Notice Requirements
- Miscellaneous Preservation Issues

TROUBLED PROPERTIES

Background

When privately-owned HUD-insured or -assisted properties become severely deteriorated or financially mismanaged, HUD must take corrective action as the responsible regulatory agency, and often as the actual noteholder following default and assignment. In enacting the "Multifamily Housing Property Disposition Reform Act of 1994" (Pub. L. No. 103–233, codified at 12 U.S.C. § 1701z–11), Congress granted HUD's request for greater flexibility in substantially revising HUD's statutory obligations with respect to properties being sold at foreclosure or from the Agency's inventory of HUD-owned properties, reducing the Agency's preservation duties but still requiring some minimum standards and procedures. Starting in 1995, in large part to save budget authority, Congress provided even greater "flexible authority" (12 U.S.C. § 1715z–11a(a)) for HUD's foreclosure and disposition activities, later adding authority to HUD to provide "up-front" repair grants from the Insurance Fund to purchasers of HUD-owned properties. In 1996, HUD revised its disposition regulations (24 C.F.R. Part 290) to implement the 1994 statute. In 2000, Congress first explicitly required renewal of Section 8 contracts at a foreclosure or disposition sale for projects primarily occupied by the elderly and disabled, unless "infeasible" (Pub. L. No. 106–377, § 233 (October 27, 2000)), and renewed that mandate for fiscal year 2002. Pub. L. No. 107–73, § 212 (November 26, 2001). Also in 2000, the Congress extended indefinitely HUD's authority to make up-front grants for rehabilitation (Pub. L. No. 106–377, § 204), and later amended the "flexible authority" statute to require transfer of HUD-owned properties to State or local government where the project is unoccupied or there are more than 25 percent severely defective units. Pub. L. No. 106–554, App. G, § 141, 114 Stat. 2763, 2763A—614–617 (December 21, 2000).

Issues Raised By HUD's Policy and Practices

HUD has essentially pursued policies of dumping the troubled properties on the private market, much as was done in the 1970's. Since 1995, HUD's customary approach has been to dispose of as many properties as possible and cease any Federal responsibility after the point of foreclosure:

- By terminating any Section 8 contracts at or before foreclosure (despite form contract language that the contract survives foreclosure), either during their term or at expiration, and refusing to permit assumption of project-based contracts by foreclosure sale purchasers, even willing public agencies or nonprofit bidders.
- Possibly by adjusting bidding practices to "low-ball" bids below outstanding debt and thus avoid taking title to properties at foreclosure and reselling them through the property disposition program (with its more appropriate process, rules, and grant resources).

- By selling properties at the foreclosure sale without repair or purchaser qualification requirements, restrictions, or subsidies adequate to preserve and improve properties as long-term affordable housing for Section 8-eligible families.
- By selling properties at the HUD-owned disposition sale without repair or purchaser qualification requirements, restrictions, or subsidies adequate to preserve and improve properties as long-term affordable housing for Section 8-eligible families, or by permitting demolition without regard to regulatory criteria.

HUD has never published any rules describing how it proposes to use its "flexible authority" to override its responsibilities under the 1994 statute and 1996 regulations. Similarly, we have seen no published guidelines to implement the 2000–2001 requirement to preserve project-based Section 8 contracts at elderly and disabled properties.

Since 1995, HUD apparently has not produced any comprehensive data or reports for the properties are disqualified from the program, or sold through foreclosure or property disposition. Such annual reports on June 1 of each year detailing many related issues are required by the 1994 Act, 12 U.S.C. § 1701z–11(*l*). Yet no one knows how HUD has exercised its existing authority to preserve properties, or the results of its decisions for affected properties, for surrounding communities, and for the residents.

Examples

Even in instances where tenant or community organizations or public agencies have demonstrated substantial support for preserving and improving these properties, HUD has refused to explore alternatives that would preserve and improve viable properties as housing affordable for the extremely low-income families served by Section 8. The following are specific cases that have come to our attention, but more detailed oversight would likely produce additional information.

Rotella Park Manor (Thornton, CO)

This 100 percent Section 8 property in substandard condition was scheduled for foreclosure sale. The Colorado Housing Finance Authority should acquire the property and preserve the project-based Section 8 contract while financing the purchase and rehabilitation, either as lender or as purchaser. Despite this request, backed by significant technical information and community support, and despite its "flexible authority," HUD refused to permit the transfer of the Section 8 contract. The State agency purchased property, but the subsidy has been converted to vouchers, jeopardizing the viability of a substantial State investment if the market softens, and removing the property from guaranteed use for very-low income families. Most of the units will not pass the necessary housing quality inspection until completion of rehabilitation.

Brick Towers (Newark, NJ)

Tenants have been fighting to save this 324-unit property for years. The residents have established a nonprofit corporation and entered into a joint venture with a reputable developer who has lined up private financing for a $10 million rehabilitation, using Tax Credits and perhaps preserving the Section 8 contract, which has not yet been terminated (as of early September). Despite solid community support for preserving the property (City Council has passed resolutions and in June 2002 enacted an 18-month moratorium on demolition; Federal legislators and local public officials have written in support), HUD plans to give the buildings and $12 million to the Newark Housing Authority, which plans to demolish them, and redevelop a lesser number of units on the site for mixed-income use. The residents' plan would preserve 324 affordable housing units, avoid the involuntary displacement of hundreds of African-American families and save taxpayers $12 million. HUD gave the NHA repeated extensions to close the transfer (scheduled for around September 13), while refusing to discuss the merits of the residents' proposal.

East Liberty Properties (Pittsburgh, PA)

In Pittsburgh, a community effort to redevelop three troubled projects (the former "Federal American" properties in East Liberty) proposes to demolish the existing buildings (three high-rises and adjacent low-rises, all of which are obsolete and physically deteriorated), and construct a number of less dense, mixed-income residential developments, on the existing sites and on other nearby sites. Two of these properties were recently processed through the "Mark-to-Market" Program, while another remains in default on its first mortgage, and awaits foreclosure and disposition. This effort enjoys broad support among the local community, city officials, and a coalition of resident organizations in the properties. However, that support—and

to some extent the viability of the development plan itself—is threatened by HUD's refusal to allow a transfer of the existing project-based Section 8 contracts to newly developed replacement housing, even where that housing is constructed prior to the demolition of the existing structures.

Satsuma Gardens (Pasadena, TX)

HUD sold this 232-unit property at foreclosure on August 28 to a for-profit developer on the courthouse steps with virtually meaningless affordability restrictions on only 79 units. Tenants were entitled to 60 or more days notice. No one knew about it because HUD had provided a notice dated June 27, 2000, stating that HUD intends to foreclose "within the next few months," but then delayed the sale for more than 2 years. The notice failed to comply with HUD's own regulations, by not indicating the deadlines for offers or any comments, and failed to state that the full disposition recommendation and analysis and other supporting information would be available for inspection and copying at the HUD field office (per 24 C.F.R. § 290.11(d)). The notice also stated that the complex (not just 79 units) must be maintained as affordable housing for low-income persons for 20 years, while the actual 2002 sale imposed no restrictions on the remaining 153 units. At least three nonprofits were interested in possible acquisition.

Village of Eastgate (Garland, TX)

This 878-unit property is 98 percent occupied and in good shape. HUD sold the property to the City of Garland for $1 in 1996, requiring that it be kept as affordable housing for only 7 years. The City plans to demolish it with the hope of major hotel development.

Ellison Apartments (Red Bluff, CA)

For many years, by its blatant failure to exercise oversight, HUD contributed to this property's troubled status (default on mortgage, serious and pervasive HQS problems, drug activities). Rather than working with the community, HUD tried to auction it off at foreclosure without preserving affordability and ensuring needed repairs. This project represented 12 percent of all the affordable housing in Tehama County, one of the poorest counties in California. This project was also a critical source of housing for individuals protected by the Fair Housing Act. After months of concerted advocacy by tenant leaders, community groups, and city and Federal executives and legislators, along with threatened litigation, HUD finally agreed in 2000 to bid its full debt to acquire the property at the foreclosure sale, and transfer it to the city with an up-front grant for resale to a community-based nonprofit for rehabilitation.

HUD APPROVAL OF PREPAYMENTS ON PROPERTIES REQUIRING HUD APPROVAL

Prepayment of a Federally-subsidized mortgage terminates the regulatory agreement and the accompanying Federal use restrictions on rent levels and occupancy. While many HUD-subsidized developments are eligible for unrestricted prepayment under statutes passed since 1996, many other properties cannot be prepaid without HUD approval. These include properties originally owned or still owned by nonprofits, many properties with Flexible Subsidy restrictions, and properties with Rent Supplement or Section 236 RAP contracts. HUD's approval decisions are governed by Section 250 of the National Housing Act, passed in 1983, which requires HUD to undertake a specified process and make certain findings, including that "the project is no longer meeting a need for rental housing for lower-income families." HUD has published no regulations or other administrative guidelines to implement this statute. Yet, in an unknown number of cases, HUD has approved prepayment for these properties without making the required findings. Despite the fact that Congress amended Section 250 in 1988 to remove its authority to do so, HUD has specifically allowed the availability of "other Federal assistance" such as tax credits and enhanced vouchers to influence its approval decisions under Section 250. These prepayments often result in restructuring rents at affected properties at higher levels at or near market at considerable public expense. While some existing tenants may receive vouchers, many will experience significant rent increases even with the voucher. In any case, these prepayments remove units from availability to very low-income families in need of affordable housing that cannot afford the higher rents.

Examples

At least three such prepayments under Section 250 have occurred in the past few years (two in Texas and one in California). HUD has never published or otherwise explained its policy and how it complies with Section 250, nor accounted for its specific approval decisions.

Bryte Gardens (West Sacramento, CA)

HUD approved a prepayment and transfer plan for this Section 236 property that was originally owned by a nonprofit and sold to a for-profit owner in 1982. Using tax credits and bond financing, a new purchaser obtained HUD approval for a new rent structure based on the tax credits, which approximate market rent levels in the area, memoralized in a HUD "Use Agreement." HUD made no findings required by Section 250 regarding the current and the future need for the property under its current Section 236 subsidized status, instead creating its own illegal standard of accepting a Use Agreement. Nor did HUD make any effort to ensure that the owner had complied with applicable State law concerning prepayments. About one-third of the tenants have experienced rent increases, and some in excess of $200 monthly. A Federal court's refusal to enjoin the transaction and dismissal of the case as moot is now on appeal to the Ninth Circuit.

REVISION OF FLEXIBLE SUBSIDY AGREEMENTS

Many of HUD-subsidized properties (reportedly more than 60,000 units) received assistance under the Flexible Subsidy program in the late 1970's and 1980's to address physical needs or other financial difficulties. In exchange for this assistance, many owners signed form Flexible Subsidy Assistance Contracts that prohibit prepayment of the insured or subsidized first mortgage note without HUD approval, and require the owner to execute an amendment to the note. Presumably, such prepayments should be governed by the standards and procedures of Section 250, *supra.* The Assistance Contract also required the owner to maintain the low- and moderate-income character of the project for the full remaining mortgage term, including compliance with all of the provisions of the applicable program (usually Section 236 or Section 221(d)(3) BMIR) and the regulations, the heart of which was budget-based, HUD-regulated rents. Usually, HUD also required owners to execute a Flexible Subsidy Use Agreement imposing identical or similar obligations.

Over the past few years, HUD has renegotiated Use Agreements on some of these properties, sometimes involving prepayment of the mortgage, again with no published standards and apparently little public scrutiny. The Agency's compliance with Section 250 for any related prepayments remains unclear. An appropriate policy might allow HUD to approve prepayments and renegotiation of the Use Agreements in exceptional circumstances for clearly defined preservation transactions where trade-offs are justified due to increased affordability terms (including restricted tenant-endorsed nonprofit ownership), no harm to current and future tenants, and full utilization of and duty to accept project-based Section 8, etc. Because no policy has been published as a rule, Congress should request HUD to explain its policy and its specific decisions, and why the policy has not been published. In addition, Congress should investigate whether HUD has approved any new rent restrictions on properties formerly restricted by budget-based rents, other than those specifically contemplated under the Section 8 "Mark-Up-to-Market" Program, as well as the Agency's asserted authority and reasons for doing so.

HUD'S FAILURE TO IMPLEMENT THE SECTION 531 REHAB GRANT PROGRAM

About 5 years ago, in Section 531 of MAHRAA (Pub. L. 105–65), the Congress directed that authority for Interest Reduction Payments on Section 236 properties with IRP contracts terminated through prepayment or foreclosure be recaptured and used for rehabilitation for eligible multifamily projects. In late 1999, HUD had developed a Draft Notice to make this IRP Pool Fund available, but it was never issued. Despite its inclusion in the fiscal year 2001 and 2002 budgets, HUD never implemented this grant/loan program, and Congress recently rescinded $300 million for antiterrorism activities. Both the fiscal year 2003 Budget and the Senate Appropriations bill project another $100 million being made available in the coming year. Congress should require that HUD take the necessary steps to immediately make these funds available, to provide important new incentives, coupled with new use restrictions, to preserve and improve properties still at-risk of conversion to market rate.

PROVIDING ENHANCED VOUCHERS TO OWNERS WHO VIOLATE NOTICE REQUIREMENTS

Background

Federal law (42 U.S.C. § 1437f(c)(8)) requires a 1-year written notice with specific content prior to contract expiration or termination. In the Section 8 Renewal Policy Guide (January 2001), following a 1999 Federal court decision, HUD clarified that owners seeking to opt-out must clearly state that intention. The statute also specifies that the owner must not evict the tenants and cannot increase tenant rents until 1-year after proper notice is provided, and authorizes HUD to offer noncom-

plying owners a renewal contract on HUD-set terms and conditions until proper notice is served and the applicable period has run. However, HUD has often provided enhanced vouchers at scheduled contract expiration to properties where owners have not provided legal termination notices, effectively providing financial rewards to owners for violating the law, while permitting simultaneous compliance with the statutory rent limits. Where valid notice has not been provided, the contract expiration date has passed and the owner has not executed a renewal contract, HUD has declined to provide renewal contracts to the current owner or to a preservation purchaser.

Last fall, the Chairman and several other Senators wrote to Secretary Martinez requesting that HUD provide enhanced vouchers only where the contract has been validly terminated with proper notice, but received no definitive written commitment to cease this practice.

OTHER PRESERVATION ISSUES

Congress Should Require HUD to Pursue an Overall Policy Favoring Preservation and Create an Office of Preservation to Coordinate HUD Efforts

If Congress establishes or encourages HUD to more actively pursue a Federal preservation policy, it should consider establishing a responsible official within HUD to coordinate the Agency's efforts to ensure that the various programs and officials work toward that objective.

Mortgage Sales

Since the mid-1980's, HUD has sought to raise revenue while divesting itself of oversight responsibilities by selling HUD-held multifamily mortgages to private lenders or to the project owners themselves. Because such note and mortgage sales can strip away Federal regulatory protections such as rent and occupancy restrictions, courts enjoined such policies and Congress enacted statutory restrictions on such policies for subsidized properties in 1988. It is unclear whether HUD is taking the position that its recent "flexible authority" (12 U.S.C. § 1715z–11a) relieves it of any obligation to comply with the 1988 statute and implementing regulations governing mortgage sales. Yet it appears that HUD is selling HUD-held mortgages on "unsubsidized" properties with no regard to the impact of such sales on the continuation of existing protections for tenants and the affordability of the housing in the regulatory agreement. Many such "unsubsidized" properties were not "deregulated" and apparently still have budget-based rent restrictions. HUD should not be selling these mortgages in a fashion that fails to protect tenants or housing affordability.

No Efforts to Transfer Disqualified Properties to Nonprofits

In Section 516(e) of MAHRAA, for properties disqualified from approval from a restructuring plan because of prior program violations by the owner, the Congress directed HUD to "establish procedures to facilitate the voluntary sale or transfer of a property" as part of a restructuring plan, with a preference "for tenant organizations and tenant-endorsed community-based nonprofit and public agency purchasers meeting" reasonable HUD-established qualifications, thus preserving the Section 8 contract and providing for necessary rehabilitation of the property. HUD's regulations provide only that any such owner facing disqualification provide a notice to nonprofit organizations if they are intending to sell the property. Not one of HUD's other powers as insurer or holder of the mortgage or as contract administrator on the existing Section 8 contract are brought to bear upon the proposed disqualification or the owner's intent to hold the property. Congress intended that HUD do more to "facilitate" transfers of these properties than sit on the sidelines and watch owners do whatever they choose, unencumbered by other HUD leverage such as foreclosure, taking possession, pursuing other contract remedies, or seeking civil money penalties.

Providing Federally-Insured Financing for Preservation Purchasers

Nonprofits seeking to purchase properties with expiring below-market Section 8 contracts at-risk of conversion can often take advantage of the Federal "Mark Up" in Section 8 contract rents as a vital preservation tool, increasing project income. However, because the Federal subsidy commitment is limited to 1-year at a time, obtaining financing to purchase and rehabilitate the property is often extremely difficult, forcing resort to public agencies or to underwriting properties at lower rent levels (that is, tax credit rents). More grants or deferred loans from public agencies are therefore required to complete the financing package. HUD should consciously provide Federal mortgage insurance for the security that most lenders require, and

allow preservation purchasers to take full advantage of the higher Section 8 subsidies to save scarce State and local resource and thus preserve more properties.

Implementation of a Rent Consistency Policy so that Project-Based Renewal Offers Are Comparable to Enhanced Voucher Rents

On numerous occasions, it has been reported that "market rent" levels determined by the required Rent Comparability studies for the renewal of expiring Section 8 contracts were less than those same "market rents" available under the enhanced voucher program to owners who opt-out. These two rent levels substantially affect an owner's decision to remain in the program or opt-out, but are determined by different agencies and personnel. Consequently, owners who can get more rent under the voucher program had no incentive to remain in the project-based program. In Section 613 of the "Mark-to-Market Extension Act" last January, Congress required HUD to develop procedures to ensure that the rents being offered owners to stay in the Section 8 program are comparable to the "enhanced voucher" rents supported by PHA's and Federal subsidies when they "opt-out." Congress should require HUD to report on the steps it has taken to address Congress' directive, and a timetable for completion of its policymaking process to end this inexplicable dichotomy.

Congress Should Direct HUD to Restart the ITAG and VISTA Components of Technical Assistance Program

In Section 514 of MAHRAA, Congress recognized that tenant participation in the renewal and restructuring process for properties with expiring contracts was an essential feature of the program, and authorized HUD to provide up to $10 million annually to support outreach and tenant participation in the future of their homes. Congress reiterated the importance of technical assistance in the Mark-to-Market Extension Act. For more than a year, in the wake of unfounded allegations concerning HUD's compliance with the Anti-Deficiency Act, HUD has failed to take the necessary steps to reactivate two important components of the program: The VISTA program providing outreach and support to tenants in eligible properties, and the Intermediary Technical Assistance Grant Program, providing primarily grants for predevelopment and resident capacity building. HUD has also unnecessarily expended almost all of the fiscal year 2002 technical assistance program funding to re-record prior commitments to address what the HUD Inspector General found were nonexistent ADA violations.

Congress should ensure that HUD takes immediate steps to restart these important program components, and develops a workable plan to commit fiscal year 2003 appropriations as soon as they are available for all program components, including the Outreach and Technical Assistance Grantees who contracts expire toward the end of 2003.

Thank you, Mr. Chairman and Members of the Subcommittee, for requesting our views on the preservation issue.

PREPARED STATEMENT OF KATHERINE G. HADLEY

COMMISSIONER, MINNESOTA HOUSING FINANCE AGENCY

ON BEHALF OF THE

NATIONAL COUNCIL OF STATE HOUSING AGENCIES, WASHINGTON, DC

OCTOBER 9, 2002

Chairman Reed, Senator Allard, and Members of the Subcommittee, I am Kit Hadley, Commissioner of the Minnesota Housing Finance Agency. Thank you for this opportunity to testify on behalf of the National Council of State Housing Agencies (NCSHA).

The NCSHA represents the Housing Finance Agencies (HFA's) of the 50 States, the District of Columbia, the Commonwealth of Puerto Rico, and the U.S. Virgin Islands. I am a Member of NCSHA's Board of Directors.

State HFA's allocate the Low-Income Housing Tax Credit (Housing Credit) and issue tax-exempt private activity bonds (Housing Bonds) to finance apartments for low-income renters and mortgages for lower-income first-time homebuyers in nearly every State. They administer the HOME Investment Partnerships (HOME) program in 40 States to provide both rental and homeownership assistance for low-income families. Many State HFA's administer other Federal housing programs, including Section 8 and homeless assistance.

State HFA's have helped more than 2.2 million lower-income families buy their first home with a Mortgage Revenue Bond (MRB) mortgage. State HFA's have financed more than 2 million rental apartments for low- and moderate-income families, including more than 1.4 million apartments for low-income families with the Housing Credit. They have provided another 220,000 low-income families homeownership and rental housing help through HOME.

HFA's also administer many programs to help preserve affordable rental housing. They finance property acquisition and rehabilitation and provide owners incentives to maintain their housing as affordable or transfer it to entities that will. Many States have added preservation to their criteria for determining which developments receive Housing Credits. Some have set aside a portion of their Housing Credits for preservation.

State HFA efforts to produce and preserve rental housing received a boost from Congress' recent passage of a near 50 percent increase in the Housing Credit and Bond volume caps. However, these increases were not enough even to restore the purchasing power these programs had lost to inflation since Congress imposed the caps in 1986. Demand for Housing Credits and Bonds still outstrips their supply in virtually every State.

The availability of scarce Bond financing is severely threatened by the MRB 10-Year Rule. The rule requires HFA's to use MRB mortgage payments to retire the MRB, rather than make new mortgages to lower-income families, once the MRB has been outstanding for more than 10 years.

This obsolete rule puts increased pressure on the already inadequate Bond cap by forcing States to use new Bond authority to finance MRB mortgages, rather than recycling old authority into new mortgages. In 3 more years, the rule will have wiped out the equivalent of the Bond cap increase and will have crowded out multifamily housing lending as greater amounts of new authority are committed to single-family use.

The Housing Bond and Credit Modernization and Fairness Act, S. 677, repeals the MRB 10-Year Rule and makes other important changes in the MRB and Housing Credit programs to assure their usefulness in all parts of the country, particularly in very-low income, predominantly rural, areas. Seventy-six Senators have cosponsored S. 677.

I encourage you, Mr. Chairman, and Senator Sarbanes, to join them in cosponsoring this important bill. I ask all Members of the Subcommittee to communicate to the Senate Leadership and Finance Committee Chairman Baucus (D–MT) and Ranking Member Grassley (R–IA) the urgent need to include S. 677 in a viable tax bill this year.

Thank you, Mr. Chairman, for your strong and consistent leadership on affordable housing matters. NCSHA commends you for holding this hearing on affordable housing preservation.

The need to preserve affordable rental housing goes hand-in-hand with the need to produce more of it, about which NCSHA testified before this Subcommittee 2 weeks ago. The same urgent needs that demand the production of more affordable rental housing make it imperative that we protect the existing affordable rental housing stock.

In its much anticipated, recently released report on Federal housing policy, the Millennial Housing Commission concluded, "it is critical that the Nation adopt a preservation philosophy to guide its housing policy going forward." We wholeheartedly agree and stand ready to help.

The Housing Need is too Great to Allow the Loss of Stock

There is an ever-growing consensus, supported by academic research, newspaper reports, and the personal experience of millions of low-income families, that our Nation confronts a deepening affordable housing crisis. According to the 1999 Annual Housing Survey, one in seven American families has a severe housing problem, meaning they spend more than half their income on housing or live in substandard housing. That is 15.5 million families, both homeowners and renters.

This housing crisis extends from the very poor to the solidly working class. Indisputably, those hardest hit are those with the least income. Of the 15.5 million families with severe housing problems, 80 percent are very-low income, earning 50 percent of their area's median income (AMI) or less. Nearly 60 percent have extremely low incomes, earning 30 percent of AMI or less.

With so many families in urgent need of affordable housing, we cannot afford to lose a single unit of affordable housing. Yet, we are losing staggering numbers of units. According to HUD's 2001 report on worst-case housing needs, in 1999, the Nation had nearly 1 million fewer apartments with rents affordable to extremely low-income families than in 1991. Between 1997 and 1999, the number of apart-

ments affordable to extremely low-income families declined by 750,000, or 13 percent. During the past 4 years, nearly 150,000 Federally-assisted units have been lost to mortgage prepayments or owner opt-outs. The threat of further losses looms as subsidy contracts on hundreds of thousands of units expire each year.

Substantial New Federal Resources are Needed

A substantial part of the problem is that we are not allocating enough resources to replace housing we lose, repair deteriorating units, and subsidize tenants to help them pay otherwise unaffordable rents. More Federal resources must be devoted to producing and preserving affordable rental housing, especially for those with the least income. Changes in the voucher program, such as those Senator Sarbanes' bill, S. 2721, proposes, are also needed.

Instead of increasing housing resources, however, the Federal Government has reduced them. Today's HUD budget is a third of what it would have been had it kept pace with inflation since 1976. The HUD budget has remained flat in nominal terms over the last 27 years. It has barely grown from $29.2 billion in 1976 to $30 billion in 2002, losing nearly two-thirds of its purchasing power. During the same period, total Federal discretionary budget authority has grown from $194 billion to $635 billion, a threefold increase.

This year, Congress rescinded $300 million that could have been used to rehabilitate affordable apartments in need of repair and another $400 million that otherwise could have helped families pay unaffordable rents.

Increased funding for existing HUD programs is essential. However, funneling more resources into these programs alone will not eliminate the affordable housing shortage. New Federal subsidy sources are needed to leverage and extend the reach of existing programs.

To respond to the growing need for affordable rental housing and to prevent its further loss, NCSHA advocated in testimony before this Subcommittee 2 weeks ago the creation of a new source of flexible Federal funds administered by State HFA's to produce and preserve rental housing targeted to extremely low-income families. We urge you to move quickly to enact this program. In the meantime, we ask you to direct HUD to take several immediate steps to preserve affordable units that might otherwise be lost.

HUD's Section 8 HAP Ruling is Wrong and Will Increase Opt-Outs

One of the most urgent preservation issues confronting HFA's arises from HUD's recent ruling that certain Section 8 Housing Assistance Payments (HAP) contracts terminate upon the refinancing of the mortgages they support. This ruling, which HUD is on the verge of implementing both prospectively and retroactively, will enable hundreds of owners to opt-out of Section 8 contracts believed to guarantee the affordability of the housing they support for another 10 or 20 years.

We urge you to stop HUD from implementing this ruling. If HUD refuses, we ask you to pass legislation protecting the contracts in question for their full terms.

The contracts in question were written between 1975 and 1980, a period of significant Section 8 activity. HUD estimates that the contracts support more than 1,000 properties with as many as 150,000 apartments. NCSHA's survey shows that more than 1,300 contracts are involved. At least 278 of these contracts covering 25,000 apartments support mortgages that have been refinanced.

HUD's ruling came after the New Jersey Housing and Mortgage Finance Agency (NJHMFA) and an owner of a property financed by NJHMFA agreed in principle to refinance the NJHMFA mortgage and assign the associated HAP to the new mortgage, as had been done in hundreds of refinancings over the last 20 years. HUD reviewed the refinancing plan, as it always has done.

In reviewing the New Jersey property's refinancing plan, a HUD lawyer interpreted a clause of the Section 8 HAP contract to mean the contract terminates on the date of prepayment of the original mortgage. The clause states the contract term shall not exceed "(1) _____ years (typically 30 or 40) or (2) . . . a period terminating on the date of the last payment of principal due on the permanent financing."

The HUD lawyer opined that a refinancing requiring the pay-off of the mortgage's outstanding principal balance activated the second provision of this clause, thus terminating the contract. State HFA's, owners, lenders, and even HUD field offices had long understood this provision to mean the date the last payment of principal was due under the terms of the original mortgage, not the date of prepayment of that mortgage caused by a refinancing.

NCSHA, several HFA counsel, and a number of other lawyers with substantial Section 8 expertise disagreed with HUD's opinion and urged HUD's Office of Housing and General Counsel to reverse it. We argued that the only function of the words "date" and "due" in the disputed language is to make clear that the reference

is to the full term of the original financing. Otherwise, the provision would simply read, "a period terminating on the last payment of principal on the permanent financing." The addition of the concept of the "date" on which principal is "due" makes clear the language refers to the duration of original mortgage.

For contemporaneous evidence that this is the meaning of the clause, one need only look at the regulations that applied to State agency financings at the time they entered into the contracts. The relevant section (Section 883.206(a)) of the regulations applicable to State agency projects at the time provides:

> Since the Contract under which the housing assistance payments are made concerns a project financed by a loan or a loan guarantee from a State agency, *the total Contract term may be equal to the term of the HFA financing,* not to exceed 40 years for any dwelling unit. *[Emphasis supplied.]*

HUD itself wrote the contract with the disputed language and published it in the *Federal Register* with the regulation just cited. One has to place an extraordinary burden of proof on anyone who would interpret the HUD-written contract to disagree with HUD's own regulation.

In addition, the Annual Contributions Contract (ACC) between HUD and the HFA includes nearly identical language stating, the total contract term shall not exceed the shorter of "(1) _____ years (typically 30 or 40) or (2) . . . a period terminating on the date of the originally scheduled maturity date on the permanent financing." This language proves the intent that the contract term coincide with the term of the financing.

NCSHA further supported our interpretation of the contract clause by providing HUD memoranda between HUD local offices and headquarters concerning the refinancing of a Virginia property showing that HUD had considered whether any provisions in the HAP or related documents triggered a reduction in the term of the HAP. HUD found none.

A HUD field office memorandum requesting headquarters' review and advice asked if the Section 8 owner could refinance the mortgage and assign its HAP contract without adversely affecting the provisions of that contract. The HUD field office memorandum also stated that the HFA involved in the refinancing did not want to undertake any action that could trigger a reduction of the term of the HAP. HUD headquarters responded as follows:

> We have previously stated that the statute and the regulations do not *require* a reduction in the term of the HAP Contract where State agency participation in the ownership or financing of a project is terminated by reason of a transfer of ownership or refinancing. Where HUD approval of an assignment of the HAP Contract as security for financing is requested . . . HUD approval cannot be conditioned on either reduction of the term of the HAP Contract or of the maximum housing assistance commitment. This requirement does not provide an opportunity to amend the HAP Contract or to impose new conditions. *[Emphasis in original.]*

One might question why HUD's guidance did not refer specifically to the HAP language currently at issue in concluding that the refinancing transaction did not shorten the contract's term. The answer is simply that no one in HUD's Office of General Counsel or any other office in HUD—and no one outside the Department—interpreted the HAP language as causing a termination. HUD was not unaware of the language. The correspondence makes clear that the HUD lawyers reviewed all of the documents and applicable program requirements.

Moreover, at this time, HUD was closely analyzing refinancing proposals to determine if it could cut back on outstanding Section 8 commitments. It is significant that, in this period of intense HUD scrutiny for the purpose of reducing contractual obligations, HUD did not put forward the interpretation of the HAP language it is now advancing.

The NCSHA also supplied HUD correspondence between HUD's Minneapolis field office and my agency revealing HUD had determined in 1984 that a refinancing allowed it to reduce the term of the contract. Significantly, though, HUD did not conclude at the time that it could terminate the contract. (In 1987, HUD reversed itself, determining that it was no longer necessary to reduce the term of the contract and ratifying that the contract endures through the refinancing.)

HUD's Office of Housing and its Office of General Counsel have had many occasions to consider the effect of refinancings on HAP contracts, both prior to the cited correspondence and subsequent to it. Yet, neither office has ever suggested the HAP terminates upon a refinancing until now. The hundreds of HUD personnel involved in reviewing these transactions over many years were not derelict in their duty.

They, and thousands of outside parties involved—lawyers, investors, and HFA's—were reading the contracts and supporting documents correctly.

Despite the evidence invalidating the HUD lawyer's opinion, HUD's General Counsel on June 23 issued an opinion confirming it. The General Counsel found HUD's decision to rewrite in 1980 the disputed contract language sufficient evidence that HUD believed that the original contract language terminated the contract in a refinancing and corrected it so contracts could be continued to their full terms. The 1980 version of the HAP contract states that the total contract term shall not exceed the shorter of "(1) _____ years (typically 30 or 40) or (2) . . . a period terminating on the date of the originally scheduled maturity date on the permanent financing."

Yet, HUD provides no evidence that it rewrote the contract provision to change its meaning. It is much more plausible that HUD rewrote the language to clarify and confirm the interpretation that has guided its actions and those of its stakeholders since. There is not one opinion, memo, notice, handbook, letter, or any other form of internal or external correspondence or guidance to suggest HUD changed the contract because it believed the original language caused the contract to terminate upon refinancing.

HUD's Assistant Secretary for Housing John Weicher has accepted the General Counsel's opinion and is preparing to implement the ruling soon. HUD intends to give owners who have refinanced mortgages supported by the affected HAP contracts or refinance such mortgages in the future the option of: (1) Amending their contracts to extend them through the original full term; (2) entering into a new contract under current renewal terms, such as Mark-Up-to-Market; or (3) opting-out of the Section 8 program, after a 12-month tenant notice period.

Concerned about the risk HUD's ruling poses to thousands of affordable apartments and their residents and HUD's failure to consult Congress before moving forward, we alerted Congress to HUD's plans and asked it to intervene. Other groups, including the National Housing Trust, the National Low Income Housing Coalition, the National Alliance of HUD Tenants, and the Stewards of Affordable Housing for the Future have supported our efforts.

Representatives of the Moody's Investors Service and Standard and Poor's rating agencies also have weighed in with concerns that HUD's ruling could disrupt the market for Section 8 bonds and undermine ratings on State housing bond programs. Even if HFA's are successful, as they were in the New Jersey case, in persuading owners to stay in the program, owners who choose 1-year renewals place HFA bonds issued with the backing of long-term Section 8 contracts at-risk. HFAs' bond ratings could suffer and their costs of doing business could increase—costs that ultimately will be borne by the low-income families HFA's exist to serve.

Mr. Chairman, you, Senator Sarbanes, and several other Members have asked HUD to reconsider its ruling. Yet, in a recent meeting, HUD told NCSHA it would not reverse it. Alternatively, we have suggested to HUD that it join NCSHA in devising legislation clarifying that these contracts are to extend for their full term. We have supplied HUD suggested language, which we understand HUD is currently reviewing.

Failing enactment of such legislation, HFA's may be forced to litigate this matter and ask the courts to reverse HUD's ruling or prohibit HUD from implementing it. While no HFA's want to take this action and, to the best of my knowledge, have not yet, it may be their only way to resolve this issue. I urge you to help convince HUD to avoid this legal battle by reversing its opinion or working with you to devise legislation that clarifies that these contracts are to extend for their full term.

What makes HUD's expenditure of time and effort on this HAP ruling especially galling is the presence of major preservation problems HUD should be addressing. Instead of using its energies implementing a ruling giving owners the ability to opt-out of the Section 8 program, HUD should spend more time in other areas where they can advance affordable housing preservation.

Additional Preservation Challenges HUD Should Address

In 1997, Congress enacted the Multifamily Assisted Housing Reform and Affordability Act to establish the Section 8 restructuring program, establish a new system for renewing expiring Section 8 contracts, and authorize a new preservation grants program using recaptured Interest Reduction Payment (IRP) subsidies from Section 236 projects. Recaptured IRP subsidies were to be used to provide critically needed repair and modernization funding for Federally-assisted low-income housing projects that otherwise lack sufficient reserves and capital to finance needed repairs. These units are home to tens of thousands of elderly or low-income Americans.

HUD never implemented this program. After HUD piled up $300 million that could have preserved thousands of apartments critically needed to meet low-income

families' affordable housing needs, Congress rescinded the money HUD had not used over the 5 years it had been authorized. We urge you to ensure that HUD implements this valuable and needed program. We further recommend that you allow non-FHA-insured properties access to this program. Currently, only FHA-insured properties are eligible, despite the critical needs of assisted properties without FHA insurance.

We are also concerned that HUD has not placed a high enough priority on preservation in its implementation of the Section 8 restructuring program. State HFA's acting as participating administrative entities under the program report that HUD's underwriting guidelines sometimes do not allow for adequate resources to ensure the property's viability into the future. Additionally, HUD's policy of placing properties on its "watch list" exposes them to financial risk with little HUD oversight, as the General Accounting Office recently found.

We are encouraged that oversight of the Office of Multifamily Housing Assistance Restructuring (OMHAR) now resides in the Office of the Assistant Secretary for Housing and hope that HUD will urge OMHAR to place a high priority on preservation. We support OMHAR's policy of allowing additional subsidies to support added rehabilitation to improve the chances a property will stay affordable longer than without such subsidies, but are concerned that OMHAR has not officially promulgated this policy.

Finally, State HFA's are concerned that rent adjustments available to uninsured Section 8 properties do not allow rents to rise with project expenses and may trigger defaults. We recommend Congress permit HUD to increase rents to a budget-based rent when necessary for the property to meet reasonable expenses and allow rents to rise to comparable market rents when an annual rent adjustment factor will not increase rents to market.

Standard and Poor's has downgraded several ratings on local Section 8 bond issues and is undertaking a comprehensive review of all Section 8 deals prompted by inadequate rent increases resulting from Congress' rent adjustment freeze on uninsured Section 8 properties. The current policy threatens many projects' financial condition and will lead to an increasing number of bond rating downgrades and mortgage defaults.

Mr. Chairman, Senator Allard, and Subcommittee Members, thank you for this opportunity to testify on the urgent need to preserve our Nation's affordable housing stock. The NCSHA and our member State HFA's are ready to help you in any way that we can.

PREPARED STATEMENT OF THOMAS W. SLEMMER

PRESIDENT, NATIONAL CHURCH RESIDENCES, COLUMBUS, OHIO

ON BEHALF OF THE

AMERICAN ASSOCIATION OF HOMES AND SERVICES FOR THE AGING

OCTOBER 9, 2002

Chairman Reed and Members of the Housing and Transportation Subcommittee, I am Tom Slemmer, President of National Church Residences (NCR). NCR is one of the Nation's largest not-for-profit sponsors and managers of affordable housing for seniors, including over 14,000 Federally-assisted housing units located in 25 States. I am pleased to represent the views of NCR and the American Association of Homes and Services for the Aging (AAHSA), where I serve on the Board of Directors and Chair the Housing Steering Committee.

AAHSA represents more than 5,600 mission-driven, not-for-profit members providing affordable senior housing, assisted living, nursing homes, continuing care retirement communities, and community services. Every day, our members serve more than one million older persons across the country. AAHSA is committed to advancing the vision of healthy, affordable, ethical long-term care for America. Senior housing is a critical part of the long-term care continuum. Our members, mostly faith-based organizations, own and manage more than 300,000 units of Federally-assisted housing, including the largest number of sponsors of Section 202 Supportive Housing for the Elderly.

First of all, we would like to thank you, Chairman Reed and Members of the Subcommittee for holding this very timely and important hearing on preservation, the third in a series of hearings to bring national attention to the plight of affordable housing in this country. We commend the Subcommittee for convening the recent hearings on housing production needs. As witness after witness testified, there is a critical shortage of affordable housing in local communities throughout our coun-

try. As documented by the National Low Income Housing Coalition's (NLIHC) recent study on income needs for housing, affordable housing is "Out of Reach" for most working families.

For many low-income retired older persons, this situation is compounded by their struggle to meet housing and other basic needs on a fixed income—primarily Social Security. More than 7.4 million elderly households pay more than they can afford for their housing, including 1.4 million elderly classified by a HUD 1999 study as having "worst case" housing needs (paying more than 50 percent of income on shelter or living in substandard housing). Unfortunately, most of these older persons receive no housing assistance and are confronted with multiyear waiting lists for existing Federally-assisted housing. Examples of this include:

The *B'nai B'rith International Center for Senior Services,* the largest U.S. national Jewish sponsor of Federally-subsidized elderly housing (37 facilities with over 4,000 units), indicated that it is about to open a brand new 42-unit addition to its 242-unit facility in Boston. However, if and older person is not already on the waiting list, they will not likely get admitted soon to the expanded facility. With a waiting list of over 90 applicants (representing a 2–3 year wait), the new facility will clearly be filled with those applicants already on the waiting list. Similarly, a 5-year-old facility in North Hollywood, California, has over 300 on its waiting list with an undetermined wait for occupancy; and in Queens, New York, a 20-year-old facility has a waiting list of approximately 1,500 applicants for an anticipated turnover of only 10 units per year. There clearly is a great need for subsidized elderly housing, and this need will only increase as the elderly live longer and remain healthy for a longer period of time.

The *Volunteers of America* reported that they are seeing their new HUD 202 elderly facilities lease up almost as quickly as they are opened. Throughout their coast-to-coast portfolio, the average waiting list now comes to 16 months and it is getting longer. Many of the properties have closed their list at 3 years worth of future residents. This program is filling a need that is growing rapidly regardless of where you look in the Nation.

The *Retirement Housing Foundation* (RHF) reports that many of their waiting lists, especially in Southern California, are closed because they have grown to over 1,000 names. Angelus Plaza, one of the Nation's largest affordable housing communities recently opened their waiting list and within 2 months, they received over 2,800 new applications for this downtown Los Angeles facility of 1,030 units. Currently, Angelus has only 100 vacancies per year. Pilgrim Tower East in Pasadena has 158 units but they have had to close their waiting list. Wilshire House has 72 units in Santa Monica and their waiting list is closed. MacArthur Park Tower in Los Angeles has 183 units but the waiting list had to be closed for now. Culver City Rotary Plaza has 100 units but the waiting list is closed. When the lists get this long, some older persons are forced into other alternatives which may include homelessness. In the Los Angeles area, housing costs have skyrocketed and the population of homeless women, children, and seniors has grown significantly.

In addition to concerns for the development of affordable housing to address current and projected needs (particularly important for the projected doubling of the elderly population by 2030), there is a simultaneous concern with the loss of current affordable housing. NCR and AAHSA believes that one of the most critical housing issues confronting affordable housing in this country is to stop the hemorrhage and to replace the loss affordable housing. As the Committee knows from your June 27 hearings on the Seniors Commission, preservation was designated as the top priority of the Senior's Commission and one of the major recommendations of the Millennial Housing Commission. As we seek domestic security for our country, we must also ensure a fundamental need of "housing security" for the elderly and for other special populations.

Out of concerns for the preservation of affordable elderly housing, AAHSA established this year, a Task Force on Preservation which I am pleased to Chair. We are pleased to participate in these hearings and look forward to working with the Committee to preserve the supply of affordable housing in this country.

In my testimony, I will share some of NCR's and AAHSA member's experiences with recent efforts to preserve affordable housing for older Americans. My testimony will focus on a series of local examples (short stories) that NCR and other AAHSA members have experienced which illustrate the struggle in our efforts to fulfill our mission to provide both suitable and affordable housing for older persons in the context of existing resource priorities, public policies, market forces, and Government regulations.

My testimony will focus on five major preservation issues:

I. Loss of the existing supply of affordable housing as current owners "opt-out" of Federally-assisted housing and convert these properties to market rate housing.

II. Limited funds and other barriers confronting not-for-profit organizations in their efforts to acquire potential properties to preserve affordable housing.

III. Concerns with foreclosure and refinancing of Section 202 elderly housing projects.

IV. Use of enhanced vouchers and other counter-productive policies; our housing members report that vouchers are "ouchers" for many older persons, for example, they simply do not work very well for older Americans.

V. Modernization, rehabilitation needs of "aging" buildings.

Recent Losses and Need to Preserve Affordable Elderly Housing

One of the most critical needs confronting affordable housing in this country is the need to preserve the current supply. According to the 2001 State of the Nation's Housing by the Joint Center for Housing Studies of Harvard University, more than a million units of affordable housing have been lost for low-income persons over the past 10 years (900,000 between 1993–1995 and 300,000 units between 1997–1999). In fact, there have been more affordable housing units lost over the past few years than have been produced, including rural housing through the Section 515 program, as testified at your recent hearings by the Housing Assistance Council (HAC). Additionally, the National Housing Trust (NHT) estimates that if current trends and policies continue, between 500,000 and 600,000 Federally-assisted housing units are at-risk of prepayment and potential loss to market rate. For various reasons, owners are prepaying their Federal mortgage, opting-out of Federally-assisted housing, and converting affordable housing to market rate.

Earlier this year, NHT conducted a study of housing loss. They noted that in recent years, nearly 200,000 units, in over 1,000 properties that served lower-income households, had been lost to the affordable, regulated housing inventory. In a separate study for the Seniors Housing Commission, NHT documented that owners of more than 250 properties that primarily serve the elderly (where more than 50 percent of the households were 62 or over) have prepaid in recent years their HUD FHA-insured mortgage or opted-out of their Section 8 contracts; and therefore, losing over 20,000 apartments from previously regulated affordable rents. Unless there is a change in policies and market conditions, we expect that this trend will continue since many properties that primarily serve older persons have high-interest rates with current rents below market rate.

Because of the timing, relevancy, and depth of this NHT study, "Preserving and Improving Subsidized Rental Housing Stock Serving Older Persons: Research and Recommendations for the Commission on Affordable Housing and Health Care Facility Needs for the 21st Century," we would like to request that the study be included as part of our testimony.

Efforts by Not-for-Profit Organizations to Acquire and Preserve

NCR and other AAHSA members have a mission and long-term commitment to provide suitable and affordable housing for low- and moderate-older persons, including extremely low-income persons. To achieve our mission, many AAHSA members have worked in partnership with other public and private organizations, including the Federal Government. With growing concerns over recent and potential loss of affordable housing units, NCR and other AAHSA members have sought to acquire some of these properties that are "at-risk" of converting to market rate housing—out of reach for most low-income older persons. We firmly believe that it is significantly less costly to preserve these housing units rather than to replace them. In fact, NCR experiences indicate that it costs over twice as much to replace these housing units than it does to preserve them.

As a CEO of a major nonprofit/faith-based organization, as an AAHSA Board member, as a founding member of SAHF* (Stewards of Affordable Housing for the Future—a recently established coalition of national nonprofit organizations dedicated to the preservation of affordable housing), and as a taxpayer, I have very serious concerns with the loss of the investment of public dollars in affordable housing. I am particularly concerned when I experience firsthand the consequences of the

*SAHF is comprised of eight major national nonprofit organizations that own and operate over 65,000 affordable apartments serving low-income elderly and families in 46 States and DC. Members are committed to the mission of providing and preserving affordable housing for the long-term, keeping well-maintained, and enhancing resident services for the people who call it home. Members of SAHF are: The National Housing Trust; Mercy Housing, Inc.; National Church Residencies; the NHP Foundation; NHT-Enterprise Preservation Corporation; Preservation of Affordable Housing, Inc.; Retirement Housing Foundation; and Volunteers of America.

conversion to market rate of many of these desperately needed affordable housing properties, primarily to increase the profit by their for-profit owners. I do not have a problem with for-profit owners seeking to maximize their investment in rental housing; however, I do have very serious concerns with public policies that thwart efforts by not-for-profit organizations seeking to preserve the public investment in these affordable housing properties for low-income older persons.

Yet, under current policies, NCR and other nonprofit organizations are being forced to "compete" with for-profits for the preservation of these affordable housing facilities that were developed with public dollars to assist low-income persons. Owners of Federally-assisted housing have the legal right to "opt-out" of Federal use restrictions after a specified period of time, usually in 20 years when their Section 8 contract expires, and an option to maximize their investment by converting the property to market-rate housing.

Some owners may seek to opt-out because they are tired of the bureaucratic and capricious rules and regulations of Federal programs. I can certainly relate and empathize with their frustration. However, what concerns many AAHSA members and me is that we are willing to endure the regulations and other bureaucratic complexities because we need the resources and partnership with the Federal Government in order to fulfill our long-term commitment of providing affordable housing for low-income older persons. Unfortunately, in too many situations not-for-profit organizations do not have the resources or means to compete with for-profit owners who are seeking to convert the property to market rate—even at the expense of critical affordable housing needs of low-income older persons. The typical older person residing in our facilities is an older woman living alone on a fixed income (primarily Social Security less than $10,000).

In some situations, we have been successful in acquiring and preserving properties. We are however, concerned that HUD is not often willing to provide adequate distribution or cashflow to nonprofit organizations. As a consequence, too often we have not been able to compete successfully due to a lack of adequate resources to acquire, disincentives of the existing owner to sell, including exit taxes, timing, local market conditions, bureaucratic red-tape, and other factors which have thwarted preservation efforts. As with most real estate, is it often a case of location, for example, the likely success of the converted property to compete in the local market. Older Section 236 affordable housing properties located in good market areas—in neighborhoods or communities with tight housing markets or areas undergoing revitalization, are at great risk of being lost. NHT developed documents that depict state-by-state comparisons of housing properties that have opted-out and those that are at-risk of opting-out. I would like to request that these charts be included as part of my testimony.

To illustrate real situations of some of the positive preservation efforts, as well as some of these unsuccessful efforts, I would like to cite just a few examples (short stories) of NCR and other AAHSA members' experiences with acquisitions and preservation of affordable elderly housing. NCR has documented some of these experiences in a short video which we would be pleased to provide for the Committee Members and staff to give a better understanding of the quality of some of these properties and our efforts to preserve them. It is very gratifying when we and/or other nonprofit organizations are able to preserve these affordable elderly housing properties. It is clearly a win-win situation for older persons, the local community, and the taxpayer. Here are a few examples of when the system works.

PARTNERSHIPS TO PRESERVE AFFORDABLE ELDERLY HOUSING

Colorado Plaza is a 47-unit Section 8 elderly housing community in *Manhattan,* Kansas. With support from the City of Manhattan, NCR purchased the property in late 2000, after learning that the building's 20-year HUD affiliation was about to expire and that the owner was not likely to renew the HUD contract. In this case, the former owner wanted to maintain Colorado Plaza as affordable senior housing, but he was weary of dealing with HUD red tape. Colorado Plaza is a prime example of government working hand-in-hand with the not-for-profit sector in order to maintain affordable housing. The Manhattan City Commission, along with Manhattan's mayoral administration, worked closely with NCR to bring about not only the purchase of the property, but also a smooth management transition. Procurement of the $1.5 million required to purchase the building was aided by the fact that NCR had successfully run an identical, 35-unit affordable senior community in Manhattan since 1989. Financing consisted of a combination of low-income housing tax credits, a Federal Home Loan Bank grant, and the assumption of the HUD mortgage. NCR pumped over $200,000 of renovations into the property, via previously attained tax credits.

In late 1999, NCR accepted title to two 52-unit affordable senior housing communities in *Eastern Ohio.* Formerly owned by a for-profit organization, Bridgeport Manor and Barnesville Manor operated under the Section 8 program. In what marks a milestone in the transfer of property from a for-profit entity to a not-for-profit organization, HUD approved the transfer of the two facilities to NCR, citing NCR's commitment to the preservation of quality, affordable senior housing. NCR's acquisition of these two properties was part of HUD's Re-Engineering Demonstration project. The project was created to offset the number of for-profit entities that are opting-out of the affordable housing program. In 1999, many 20-year HUD contracts expired, leaving affordable housing owners the option to either withdraw from the program or to renegotiate their contracts with HUD. In reevaluating the contracts, HUD lowers resident rent structures, thereby causing a substantial decrease in owner profit. Of approximately 169 eligible properties in Ohio in 1999, only 23 were approved for transfer by HUD. The acquisition of Bridgeport Manor and Barnesville Manor is the result of a transfer of physical assets, which amounts to a contribution to NCR from the former owner.

According to the National Low Income Housing Coalition, as of 1999, an estimated 38,000 affordable housing units had been lost to owner "opt-outs," while an additional 60,000 units have been lost due to owner prepayment of the mortgage. Prepayment of mortgages allows owners to pay off their debt and convert affordable housing to market-rate rents. On average, opt-out rents have increased 44 percent; prepayment units have increased an average of 57 percent. In the next 5 years, 66 percent of the existing Section 8 contract (14,000 sites) will expire, and in that same time, 50 percent of the housing stock in 40 States will expire and be eligible for renewal.

In the spring of 2002, NCR purchased four affordable senior communities in *North Carolina* (Charlotte, Clinton, Monroe, and Rocky Mount). Totaling 232 units, the facilities, which were spread over 500 miles throughout North Carolina, were in such a state of disrepair that they were virtually unlivable. No maintenance had been done in years. Heaters, air conditioners, and plumbing systems worked sporadically. Maintenance requests went unanswered for weeks, and were often times simply ignored. Low-income, elderly residents were forced to live in dangerous, squalid conditions. Rents were even calculated incorrectly, with many residents paying far more than the 30 percent maximum. All four communities were infested with roaches, vermin, and fire ants. In some cases, residents were forced to use their stoves as heaters. The $4.2 million acquisition of the four properties was funded through HUD and the North Carolina Finance Agency. A portion of the transaction included funds for significant renovation and rehabilitation of the aging buildings.

Yet, despite the fact that these are win-win situations, that they are politically popular and cost effective (a bargain), there are too many failures to acquire and preserve these properties for an assortment of reasons. While there are some similar factors, most of these preservation efforts are on a project-by-project situation. A few examples where these properties "have gotten away" and/or are currently caught up in negotiations are:

LONG-TERM COMMITMENT OF RENT SUBSIDY NEEDED FOR PRESERVATION

One of AAHSA's members, The Retirement Housing Foundation (RHF) formed in 1961, affiliated with the Council for Health and Human Services Ministries of the United Church of Christ, is a national nonprofit organization whose mission is to provide a range of housing options and services for the elderly and the low-income families. RHF owns and manages over 13,000 apartments in over 130 facilities in 24 States, Puerto Rico, and the Virgin Islands. In 2001, RHF initiated a successful effort to preserve 544 apartments for the elderly in three Boston projects (Symphony Plaza East and West, and the Stearns Apartments).

However, preservation efforts that began this year to acquire eighteen additional properties (approximately 2,450 units in Massachusetts and, Mr. Chairman, 265 units in your State of Rhode Island) are being thwarted by a number of technical and administrative issues. These properties are intended to be financed with tax exempt bonds, 4 percent tax credits, and assumption of existing Section 236 mortgages, "co-first" mortgage loans and 501(c)(3) bonds from MassHousing Finance Agency (MHFA). While one of the tax credit acquisitions in Massachusetts, and three of the 501(c)(3) bond acquisitions can be completed this year without any special allowances being made either by HUD or through legislative actions, there are two issues that could derail the rest of the acquisitions.

In order to raise enough money both to pay the seller an acceptable price and to fund necessary capital expenditures, each of the projects requires a new 20-year Housing Assistance Payments (HAP) contract, several of which must be Marked-Up-to-Market. The HAP contracts can be subject to annual appropriations in accordance

with the current HUD and Congressional policy. However, beneath this overarching issue, are two separate technical issues: (1) The ELIHPA; and, (2) the original HAP contract.

The ELIHPA Issue

Of the projects to be financed under the first two structures, four are subject to a Plan of Action (POA) and a subsequent Use Agreement deriving from participation in the 1994 Emergency Low Income Housing Preservation Act (ELIHPA) Program. While HUD policy provides for the discretionary granting of Mark-Up-to-Market HAP contracts for ELIHPA projects in the context of a sale to a nonprofit, conflicting statutes effectively remove that discretion by limiting renewals to 1-year terms that resulted from limitation from appropriation language. As a result, while it may be technically feasible under existing law to achieve market rents, no HAP contract for an ELIHPA project can run longer than 1-year. From an underwriting standpoint both higher rents and a 20-year term are required for a satisfactory price.

HAP Contract Mark-Up

The projects to be financed with 501(c)(3) bonds are covered under original Housing Assistance Payment (HAP) contracts that are still in effect, and as a result are technically ineligible for Mark-Up-to-Market. There is a need to remove barriers stopping efforts by nonprofit faith-based organizations to preserve affordable elderly housing.

Efforts to Preserve Section 202 Elderly Housing Facilities

The Section 202 elderly housing program has long been recognized as one of the most successful Federally-assisted housing programs, earning strong bi-partisan support for its sound management, mission to serve low-income older persons, and strong public-private partnership. There have been a number of revisions and improvements throughout its 40-year history, including significant changes over the past few years enabling the program to leverage additional resources to expand supply. The attached chart illustrates the four phases of the Section 202 program, the number of units, and characteristics under each phase.

In addition to concerns over stagnant, level-funding that the program has received in recent years despite critical need and projected demographic increases, there are several preservation issues including Section 202 foreclosures, and difficulties with refinancing options.

SALE OF SECTION 202 ELDERLY HOUSING PROPERTIES

Last summer, I testified before the House Financial Services Committee about our concerns with an unprecedented sale last year of a Section 202 elderly housing facility in Detroit. In addition to misgivings over the loss of more than 200 affordable elderly housing units, we expressed concerns that the sale of the previously not-for-profit sponsored property was sold to a for-profit (out-of-state) owner and converted to family/student housing. Since that time, at least two other Section 202's have been foreclosed and sold to for-profit owners, a second project in Detroit and one in New York.

The Detroit Experience

To date, two large Section 202 projects in Detroit totaling 532 units have been foreclosed by HUD and auctioned to for-profit developers with the result that both the buildings and their project-based Section 8 subsidies are lost forever to low-income older persons in the community. The first Section 202 "lost" is *Cathedral Towers* (formerly Cathedral Terrace) a 19-story, 212-unit, Section 202 built in 1971. Approximately 50 percent of the units are efficiencies. It was originally sponsored by the Episcopal Cathedral of St. Paul's which is located directly across the street and next to Hannan House, a four-story facility where a number of senior services and activities and providers are located.

In the 1980's, the Episcopal Diocese gave up its right to appoint the majority of the Board of Directors for Cathedral Towers. The Cathedral also sponsored Williams Pavilion, a 150-unit Section 202 that was built in the mid-1980's and has all one-bedroom units. Cathedral Towers has had a long history of management problems and as it got older and with the additional burden of having a large number of efficiency apartments, vacancies increased. Efforts by the Cathedral and senior service providers were rebuffed by a Board that seemed to be unaware of the problems they were facing and/or unwilling to take any meaningful action. The HUD Area Office has been aware of the problems for over a decade. In an effort to fill the vacant efficiency units the Administrator and Board requested permission from HUD to

rent to Wayne State University students. HUD granted this permission on a year-to-year basis.

When the State of Michigan discovered that the building was no longer being rented exclusively to older persons, it revoked the tax exemption and stopped reimbursing the city of Detroit for the real estate taxes. The city then initiated a tax foreclosure and it was at this point that HUD stepped in and negotiated a payment to the city to prevent foreclosure. HUD then placed the building in enforcement (Dallas office) and brought in its own management. However, it did not remove the Board and the Board refused attempts by the Cathedral and a coalition of nonprofit housing providers to take over control of the building and preserve it as senior housing. It was only when the foreclosure proceedings were already underway that the Board agreed but by then HUD said it was too late.

The building was sold on August 31, 2000, at foreclosure auction to Kohner Properties, a St. Louis based for-profit organization. HUD indicated that they had sent a letter to the city offering the property for a minimal amount. However, the city has never located the letter and, in any case, HUD said that the property would lose all of its project-based subsidy in the transfer (in other words, the Section 8 subsidy would be lost forever). HUD did place a number of deed restrictions on the property that, among other things, required the new owner to keep the units affordable for 20 years and give priority to seniors and the disabled. The amount offered by Kohner was less than $1 million which is less than a third of the assessed value of the property (the result was a bargain price for Kohner and a loss by the city of more than two-thirds of the tax revenues in addition to the project-based senior housing). The new owner has interpreted that to mean that they do not need to market to seniors and they have made only modest attempts to do so. Instead they have marketed to single individuals with advertising particularly aimed at students.

The second Section 202 facility sold in Detroit is *Four Freedoms,* a 22-story building with 320 units (57 percent are efficiencies) that was constructed in the 1960's, originally as a nonprofit Section 236 but later converted to Section 202. This facility has just recently gone through the foreclosure process but the high bid has not yet been accepted because of a legal dispute. This project also has had a long history of problems, including vacancies caused by the high number of unmarketable efficiency units. The result of this foreclosure will also be a permanent loss of project-based subsidies and a loss of tax revenue to the city. In these instances, it appears that HUD did not intervene to provide timely technical assistance, to provide oversight, and to take other actions to preserve the affordable housing that was quickly sold to a for-profit buyer at a price far below the assessed value. This resulted in not only losing the affordable housing project, but also compromising the integrity and long-term reputation of the program by opening a "Pandora's box" for potential future sales of other Section 202 properties. Additionally, in another pending situation, a group of nonprofit organizations are working to bring adequate resources together to purchase another failing Section 202. However, HUD is insisting on modernization resources that the group does not have while not providing any of its own resources nor agreeing to hold the foreclosure in abeyance.

LIGHTENING STRIKES AGAIN: THE NEW YORK STORY

We assumed that the Michigan situation was unique; however, before corrective legislative actions could be taken (provisions were added during the Committee mark-up of H.R. 3995 to provide nonprofits with a first right of purchase of any Section 202), another Section 202 elderly housing facility located in southwestern rural New York was foreclosed and sold this past spring to a for-profit owner. The facility, Oak Apartments built in 1987 with 40 units, is located in Alfred, New York, where there is a strong market for housing students attending Alfred University at rent that exceeds the affordable rents offered to qualified HUD residents. NCR had been contacted by the local community in New York to acquire the Section 202 property to preserve it for affordable elderly housing. However, despite our interest, organizational capacity, and local support, NCR was not able to acquire the property at a price that would have allowed it to remain affordable to low-income seniors. Although the sale from HUD to the owner included a legislative "use restriction" initiated during a previous 1983 sale to remain "affordable senior housing," it is unclear the specific terms of the restriction, what State regulatory body was is charge of enforcing the restriction, or how easily the restriction could be removed. In fact, just weeks after the sale of the property, the new owners were making inquiries on how to convert the property to student housing even after promising the community during the public comment period the property would remain affordable senior housing.

It is clearly shortsighted and not cost-effective to use public funds that were invested into these affordable housing facilities and then, despite need, to sell these facilities at significant discount to for-profit owners to convert them to market-rate

housing. Nonprofit affordable housing advocates simply cannot move fast enough to compete with market forces without more effective tools and a proactive HUD office. Not-for-profit owners must often receive approval from a majority of a volunteer board of directors, that may not be able to meet, develop an adequate market study, and vote for a purchase in the current timeline for HUD foreclosure sales. In recent years, local communities in New York lost more affordable elderly housing units through opt-outs and conversions than the State's entire Section 202 allocation to construct new units.

REFINANCING 202's AND LIMITED PARTNERSHIPS

Because of the need for funds to expand the number of units in a Section 202 elderly housing, (funding has been reduced in recent years to an average of less than 50 units per project); as well as a need for capital improvements. The AAHSA sought legislative changes to enable options to leverage Section 202 funds and equity to attract other public and private resources. This effort evolved from an earlier AAHSA supported proposal to have the Federal mortgage forgiven on pre-1990 Section 202 elderly housing facilities, as a means to de-couple the Section 8 rent subsidy and to tap the equity in the facility. But unfortunately, while a Senate requested HUD study indicated this is budget neutral (debt forgiveness off set by reduced future Section 8 payments), it would require a change in budget scoring legislation that was not politically feasible at the time.

We are pleased that Congress has made a number of reforms to the Section 202 program over the past couple years, to provide increased flexibility and financial options for attracting public and private capital for Section 202 projects. For example, with new legislative authority enacted (Pub. L. 106–569) to enable refinancing and limited partnerships between private investors and the traditional not-for-profit sponsors of Section 202 projects, it will be easier for Section 202 elderly housing sponsors to bring private financing into the development and/or refinancing of the projects. As the sole general partner of a limited partnership, not-for-profit sponsors can partner with for-profits to leverage additional funds through low-income housing tax credits, private activity bonds, and other resources used in combination with Section 202 funds.

REFINING NEEDS SPEEDY PROCESSING

In 1999, MassHousing staff developed a proposal for refinancing HUD-held Section 202 mortgages with high-interest rates. This proposal won a national award from the National Council of State Housing Agencies (NCSHA) in September 2000. At the same time, MassHousing approved the refinancing of Peter Sanborn Place, a Section 202 development in Reading, Massachusetts, that had a 30-day right to prepay without HUD's consent. The MassHousing loan will lower the interest rate for the project from 9.25 percent to less than 6.0 percent and recast the amortization schedule for 40 years. This refinancing will lower annual debt service costs for the project and generate proceeds of at least $1,049,000 above the existing debt to be used for physical improvements to the property and to establish an escrow to fund resident services. The funds generated by the refinancing will enhance the quality of life for the residents and enable them to remain in their apartments as they age in place.

Unfortunately, MassHousing has reported that they have received great resistance from HUD at both the local and national level for over 2 years in approving the refinancing. Widespread support for the proposal was received from Congressional leaders in both the House and the Senate; but it was not until this past summer (July 2002), after direct Congressional intervention, that MassHousing received a conditional approval letter from HUD. However, the letter did not resolve all policy questions nor permit flexible interpretations of the Use Agreement in the notice for HFA/FHA Risk Share refinancings. As a result, MassHousing still lacks HUD final approval for this beneficial refinancing. Clearly, if not-for-profit organizations are going to be able to refinance Section 202 housing facilities, as Congress enabled, HUD needs to provide timely leadership, guidance, and processing.

VOUCHERS ARE OUCHERS FOR OLDER PERSONS

While vouchers may be a useful tool for providing safe, decent affordable housing for low-income families, vouchers are not as effective in providing affordable housing for older persons. Vouchers (when available and acceptable by landlords) tend to focus on affordability issues through private sector, mixed-income, and scattered-sites strategies. The eligible low-income person is empowered to locate housing in the community and to use the voucher to reduce their portion of the rent by paying 30 percent of their income and having the Federal Government pay the landlord the difference.

Elderly housing is more complex and addresses multiple needs of older persons beyond simply affordable housing. One of the primary benefits of elderly housing is the fostering of formal and informal supportive services. While vouchers tend to emphasize scattered-site strategies, senior housing is project-based and works well with higher density facilities. Elderly housing provides a base for the delivery of support services that become more crucial as older persons age in the facility. Nonprofit, often faith-based housing also tends to serve as a catalyst for increased volunteers and community support.

One of the primary benefits of age-distinct elderly housing is the fostering of informal support systems for older persons, which is particularly beneficial in ending isolation for older residents, particularly since the typical resident is an older women living alone on a low and fixed income. Senior housing tends to be a catalyst for community services and often serves as a community focal point for assisting older persons in the surrounding area. From a public policy perspective, elderly housing with supportive services is very cost effective in assisting frail elderly to delay and or avoid costly institutions, such as assisted living and nursing homes. In fact, supportive elderly housing is a bargain from a comparative cost perspective.

In recent years there has been increased recognition of the emerging role that elderly housing with supportive services (and service coordinators, etc.) can have with long-term care strategies. Yet, many elderly residents have aged-in-place and are becoming more frail and at-risk of higher level of care facilities (assisted living or nursing homes). For many of these older facilities there is a need to rehabilitate or modernize to accommodate supportive services. For example, many of the Federally-assisted housing facilities were developed as "independent" housing; yet have begun to facilitate an increased number of community services.

From a preservation perspective, many of the older housing facilities, such as a Section 236 facility, are being refinanced as a means to make capital improvement to accommodate supportive service needs, including the conversion of some units to affordable assisted living. Since some older persons may prefer to live in mixed-age, family settings, a range of housing options should be available in local communities. In this situation, vouchers could be helpful to make housing more affordable. However, project-based rent subsidies work best in senior housing for older persons—affordable senior housing is an American success story.

Enhanced Vouchers: A Mixed Blessing or Trojan Horse

With concerns over the adverse impact that conversion to market-rate housing would have on existing residents, for example, being forced to pay increased rent or move to more affordable housing, Congress provided a number of protections, such as: Advance notices, moving assistance, and enhanced vouchers. And with an enhanced voucher, an existing resident in a Federally-assisted housing facility involved with Mark-to-Market would have the option to continue to remain at the facility and to continue to pay their current rent structure (for example, 30 percent of their adjusted income). The Federal Government would subsidize the qualified low-income resident's rent, but at the increased, ("enhanced") market-rate level.

At first observation, it would seem that enhanced vouchers provides a "win-win" solution enabling residents to remain in their homes and encouraging owners to continue to provide affordable housing. However, while some protection is being provided for *existing* residents, in some regards, enhanced vouchers may actually be a mixed blessing with unintended consequence of masking the extent of recent losses of affordable housing. Without enhanced vouchers, the adverse impact of dramatic increases in rents as units are converted to market rate would certainly contribute to a public outcry among existing residents and local communities. However, with enhanced vouchers, affordable housing units are gradually lost, unit-by-unit, as existing residents move out or die but generally, without public awareness.

In many ways, the enhanced vouchers contribute to a "silent crisis" with the gradual loss of affordable housing. We believe that enhanced vouchers provide only a short-term solution to accommodate affordable housing needs of existing residents. In the long run, however, they also contribute to the gradual loss of affordable housing. To illustrate this point, I would like to discuss two recent NCR preservation efforts: One in Pacifica, California, was able to acquire the at-risk property where there were no enhanced vouchers; and one in Baltimore, Ohio, where enhanced vouchers were used and we were not able to acquire and preserve for future affordable housing.

PACIFICIA, CA: RESIDENT OUTCRIES PRESERVES ELDERLY HOUSING

In fall 1998, the owners of 100-unit Ocean View Senior Apartments in Pacifica, California, a small town just 12 miles south of the Golden Gate Bridge, decided to turn the 20-year-old property into a market-rate building. The HUD loan had

been satisfied, and the owners, who had purchased the property only a year before, quietly taped 30-day eviction notices to the elderly residents doors at 2 a.m. With no affordable housing options within 60 miles, residents had no housing options, and were effectively rendered virtually "homeless." All of the residents were receiving Section 8 low-income housing assistance and the new rent rates exceeded Government standards, so enhanced vouchers were not even an option. Many of the residents suffered serious physical setbacks brought on by the stress of the situation. Needless to say, the public outcry was deafening, especially after the local newspaper, *The Pacifica Tribune,* editorialized against the owners, and in favor of maintaining the property as affordable.

In an unprecedented move, the city of Pacifica seized the property by eminent domain in a desperate move to halt the process. NCR joined the fight and quickly moved to assemble the $11.1 million needed to purchase the building and maintain it as affordable senior housing. Financing eventually came from a combination of loans and grants from the California Housing Finance Agency; the county of San Mateo; and the city of Pacifica. NCR put over $300,000 of renovations into the property. The $11.1 million purchase price was over $1 million more than the property owners had paid for the building the previous year. The Pacifica story is a classic example of the effective collaboration of residents, the general public, government, and the not-for-profit sector working together to effect positive change. NCR developed a video of the Pacifica, and a few other preserved housing facilities which we would like to include as part of our testimony.

Modernization of Older Elderly Housing Facilities

In addition to preservation needs with the loss of affordable housing facilities, AAHSA believes that there is also a critical need to preserve the existing stock of Federally-assisted affordable housing that serves moderate- and low-income households. As reported by the Millennial Housing Commission, there are 4,200 properties with 450,000 units developed between 1966–1978 under the Section 236 and Section 221(d)(d) that are now over 25 years old. Structural and mechanical systems of older building start to require significant upgrade and replacement by their 20th or 25th years.

The Section 236 nonprofit elderly developments appear to be most in need of modernization funds. During a moratorium on the Section 202 program, the only Federally-assisted program available for nonprofit organizations seeking to develop affordable elderly housing between 1969 and 1975 was the Section 236 program. As noted, the Section 236 projects have aged considerably since 1973 and are in dire need of capital for modernization. Their lack of access to adequate capital puts them at-risk of deteriorating to the extent that they are no longer viable properties. Many Section 236's have only partial Section 8 or other types of rent subsidies which could cause an adverse impact on unsubsidized tenants should rents be increased to pay for capital improvements. Depending upon the local market conditions, some Section 236's are at-risk of being converted to market-rate housing and/or are being refinanced as a means to generate funds for capital improvements.

In addition, there are over 5,000 properties with over 250,000 units that were developed with the pre-1990 Section 202 loan program—including 2,800 projects developed under "cost containment" policies (1980's) that severely limit common space, reduce amenities, use less quality materials, and emphasis on efficiencies. In addition to structural needs, many of these older facilities need capital improvements to accommodate residents' present and future service needs. These structural changes include increased common space to facilitate supportive services for older residents; converting unmarketable efficiencies into one bedroom and/or common space; retrofitting to comply with fair housing and ADA requirements; and becoming more competitive with newer and/or market-rate facilities.

A recent AARP study found that 20 percent of the oldest Section 202 facilities reported that their capital reserves are inadequate to meet current repair needs and that 36 percent reported that reserves are inadequate to meet projected repair needs. We believe that it is sound public policy to protect the public investment in Federally-assisted elderly housing facilities. AAHSA fears that ignoring these needs now will only increase affordable elderly housing needs in the near future as the health of these properties continues to deteriorate . . . "pay now, pay later."

AAHSA remains disappointed therefore, that the Administration sought and Congress concurred with the rescission in the fiscal year 2002 Supplemental Appropriations bill of over $300 million from the recaptured Section 531, Interest Reduction Payments (IRP). These IRP subsidies from Section 236 insured multifamily properties recaptured through refinancing are intended for rehabilitation grants or loans to qualified owners who demonstrate need and have insufficient project income to support rehabilitation. While HUD indicated earlier its intent to issue rules to allo-

cate these funds, to date, HUD has not yet allocated any of these IRP funds. About a quarter of the eligible Section 236 properties have elderly-headed households.

Modernization: Aging Buildings Also Need Care

The Retirement Housing Foundation (RHF) is an organization based in Long Beach, California, which has been building and acquiring housing communities for mostly low-income elderly since 1961. Some of their more than 135 properties are over 35 years old. Therefore, the process of maintaining these buildings while safely housing frail elderly can be costly over the years. Anyone who has undergone home repairs and renovation can imagine how expensive it can be to simply paint, replace fixtures, carpeting, windows, roofs, heating/AC systems, etc. Multiply those costs by 135 buildings and you are talking sizable amounts of money.

Unlike for-profit companies, RHF cannot sell off its aging buildings for a profit for conversion into market rates. Besides, that is not what our mission is about. RHF prides itself as a faith-based, nonprofit organization founded to provide a range of housing options and services for the elderly, low-income families, and persons with disabilities, according to their needs, in an environment reinforcing the quality of life as it relates to their physical, mental, and spiritual well-being. A recent poll found that the shortage of affordable housing ranks second only to health care costs as a concern for citizens.

RHF's University Center in *Indianapolis,* Indiana, which was completed in 1986, is in desperate need of upgrades and repairs. This HUD 202 senior community of 50 units recently underwent some unexpected repairs because of an "act of nature." The ground settled beneath, leaving cracks in the floors. The problem was exacerbated on the second and third floors of the building where lightweight concrete was used to provide soundproofing. The cost to fix the flooring exceeded $80,000. The parking lot needs to be repaved, cabinets need replacing (estimated cost $60,000), heaters are wearing out, and the old frost type refrigerators have outlived their useful life, not to mention being very energy inefficient. The building will need a new roof soon. Considering the needs of the facility and the lack of financial resources to make needed repairs is a dilemma for RHF and other nonprofit housing providers.

The Concord in *Pasadena,* California, a building built around 1966 has had to have its tired and weary elevators replaced at a cost of $230,000. Ralston Tower in Modesto, California, has also had to modernize elevators, which was a long drawn out costly ordeal. Pilgrim Tower East in Pasadena, California, a 158-unit bustling building of seniors was built in 1979, and the two elevators served the residents for almost 25 years before they had to be replaced. Replacement is generally due to the need for frequent repairs. Fortunately, the elevators were safe to use, however their unreliability became a nuisance to the elderly residents in the facilities. In addition, when the elevators were being repaired, the residents endured long waiting periods when trying to enter and leave their apartments. Every 5 to 7 years, common areas need to be renovated. The average cost is in excess of $25,000 per building.

RHF buildings—such as Harbor Tower in *San Pedro,* California, which was recently painted after 15 years—can look good for quite a while but they eventually need a fresh coat of paint. RHF is also in the process of investing in automatic doors for all of its buildings at a cost of $5,000 to $8,000 for each building to make access easier for frail residents and those in wheelchairs. The automatic doors are also one way to increase security. Those entering need to have a key fob or must enter a code into an entry device located outside the entrance doors. Also, in high-crime neighborhoods, an investment in security cameras and monitoring equipment has been a necessity at a cost of $10,000 or more per facility.

The true concern of nonprofit building managers is locating sufficient financial resources to address capital repairs when replacement reserve funds are either inadequate or nonexistent. That is why many housing providers have become concerned with the Administration and Congress and recent actions to divert funding away from HUD to other uses. Many housing providers try to maintain their properties for the benefit of the residents, while at the same time attempting to reduce operating expenses such as utilities. However, in order to purchase energy efficient refrigerators, water heaters/boilers, HVAC equipment, and water saving devices, additional funding is needed.

MODERNIZATION FUNDING NEEDS

B'nai B'rith Parkview Apartments (BBPA) in New York, a Section 236 project that has 118 Section 8 apartments and 59 market-rate apartments, (73 studio apartments) must maintain extremely competitive market rents to maintain a high occupancy rate. In turn, the monthly replacement reserve amount that coincides with

apartment rents made it difficult for the facility to maintain an adequate reserve needed to complete all the needed capital repairs and replacement needs.

In spring of 2002, the infrastructure of the building façade failed and bricks began falling off the 12-story building. Scaffolding was immediately placed around the building to protect the safety of the residents. Work to secure the bricks has begun and the cost of the initial stabilization of the bricks will cost approximately $90,000, or over half of their replacement reserve account. The current budget allows for $6,211 per month into the replacement reserve account. With this schedule, it would take B'nai B'rith Apartments 14 months to recoup the cost of just stabilizing the bricks to retain a minimum replacement reserve account.

Additional façade work is scheduled for next year to remove the bricks that could deplete the entire replacement reserve account. Any additional capital needs could compromise the financial stability of the project if funds are needed from the operating budget for additional capital repairs. Access to the $300 million IRP funds could have helped in preserving the replacement reserve account for B'nai B'rith Parkview Apartments for expected capital needs.

Recommendations

The NCR and the AAHSA recommend a number of actions to preserve the supply of affordable housing for older persons and other low-income persons. These include:

Establish a HUD Office of Preservation

Because of the urgency, complexities of funding, and multitude of issues to preserve the existing supply of affordable housing, AAHSA urges that HUD establish an Office of Preservation. National leadership is essential if we are not to lose virtually every affordable senior housing facility that is currently located in a good market area. The establishment of this Office would serve as a focal point within the Federal Government to provide national leadership, including a partnership with HUD local offices, national organizations, and others, to develop and administer a comprehensive strategy to preserve the Nation's supply of affordable housing. HUD already has many tools to facilitate preservation including: Data on opt-outs; mortgage insurance programs; OHMAR; vouchers; HOME funds, etc. However, NCR and other AAHSA members have had mixed experiences with working with HUD both at central and various field offices. One of the primary concerns expressed by members has been the lack of prompt action by HUD to expedite refinancing, acquisitions, and preservation efforts.

The Preservation Office should have the resources and authority to take quick actions to assist nonprofits, State and local governments, consumers, financial community, and others with resources and technical assistance to preserve affordable housing. The Office should establish special processing for HUD financing to facilitate the necessary speed of preservation transactions. The Office would also serve as a wake-up call to the silent crisis that is rapidly eroding the existing supply of affordable housing. Presently, the word "preservation" does not even appear in HUD's strategic planning documents.

Yet, this valuable housing stock is steadily and quietly being lost. Unfortunately, when the Nation comes to fully appreciate the gradual lose of this precious housing resource, it will be too late unless we do something about it now to ensure that these much needed affordable housing properties will be preserved. Once gone, we will have to start production programs to replace these units; unfortunately at a much higher overall cost to the taxpayers. We would recommend that the Subcommittee request that the General Accounting Office (GAO) conduct a study on the financial impact of the loss of these affordable housing units.

The scope of the responsibilities of the Preservation Office would be broader than the Office of Multifamily Housing Assistance Restructuring (OMHAR). The Office would coordinate and oversee preservation actions of the Office of Housing and PIH, such as assurance of compliance with Congressional mandates, promulgating regulations, and/or guidelines. Among suggested actions that the Office could take include: Technical assistance to nonprofits and others on preservation needs; facilitate with transfer of ownership, for example, opt-outs with opt-ins; develop a database of potential at-risk properties; assist States and local governments to develop preservation programs in their State (such as the establishment of Housing Trust Funds or support bi-partisan matching State program provided in H.R. 425/S. 1365) funds (grants or loans) that could be quickly accessed by nonprofits to acquire at-risk affordable elderly housing. In addition, the Office could also identify best practices and develop demonstration programs and provide incentives for existing owners to transfer ownership to a nonprofit committed to sustain affordability.

The AAHSA recommends that HUD be required to report to Congress monthly on the loss of affordable housing stock, including at-risk and lost properties listed by

Congressional district and to publish the reports in the *Congressional Record.* [We believe that it is important for Congress to realize the extent of loss and potential losses, particularly in their own local districts.] Our concern is where low-income persons will live in the future once these affordable housing properties are gone and when we consider that many of these local communities will be coming to Congress in the future to seek production programs once the voucher holders are gone. It will require significantly more tax dollars to rebuild these housing facilities than to preserve them now. It certainly doesn't make economic sense to the taxpayer and does an incredible disservice to our communities not to preserve these properties before they are converted to market rate. We would further recommend that HUD should post on its websites, information on projects that are vulnerable to market-rate conversion so that nonprofits are given ample lead times to acquire, rehabilitate, and preserve these facilities.

First Right of Refusal for Section 202's

The AAHSA recommends that statutory provision be made with the Section 202 program to ensure that any sale or disposition of a Section 202 would be to a qualified nonprofit organization. The AAHSA actively supported the provisions related to Section 202 foreclosure and sale included in H.R. 3995, the Affordable Housing for American Act, as amended. We would recommend that HUD be instructed to take prompt actions to assist current owners in preventing foreclosure, including technical assistance, adjustments to the operating budget and operational issues. However, if a transfer of ownership is still necessary or desired by the owner to prevent foreclosure or to improve operations of the facility, that HUD assist with the transfer of ownership to a qualified not-for-profit organization. The AAHSA supports use restrictions remaining with the foreclosed or transferred project until the expiration of the original term of the loan; although we would urge that some flexibility be provided to adjust the income limit (up to 80 percent of area median income) if necessary for the financial soundness of the project.

Transfer of Federally-Assisted and Rural Housing to Nonprofits

Similarly, AAHSA recommends that preference for the transfer of ownership or control of existing Federally-assisted elderly housing, including Section 515 rural housing, be given to qualified nonprofit organizations. In addition to technical assistance to assist current and potential not-for-profit owners, AAHSA recommends that HUD and USDA/RHS be directed to give priority for modernization and rehabilitation funding to qualified not-for-profits to prevent foreclosure or upon transfer of ownership to another qualified not-for-profit. AAHSA supports similar provisions that were added to H.R. 3995 for this purpose.

Incentives to Sellers

While some owners may be willing to sell or to transfer ownership to a nonprofit organization, the owner/investors are often discouraged because they would be subject to an exit tax at the time of the transfer of ownership. AAHSA supports the recommendation of the Millennial Housing Commission to provide a Preservation Tax Incentive which would grant exit tax relief to owners who sell the facility to a qualified preservation entity. While tax issues are beyond the jurisdiction of this Committee, the AAHSA would recommend that joint efforts be initiated with the Finance and other related committees to remove this tax disincentive to transfer affordable housing properties to a qualified not-for-profit organization to preserve affordable housing.

Grants for Nonprofits to Acquire Affordable Housing Facilities

The AAHSA recommends that grants be provided to assist qualified not-for-profit organizations in acquiring affordable housing for low- and moderate-income older persons. In addition to provisions that were amended to H.R. 3995 to provide operational assistance, AAHSA recommends that funds be provided for the acquisitions of at-risk properties to preserve affordable elderly housing. AAHSA further recommends that additional guidance and authority be given to HUD that not-for-profit organization seeking to acquire existing Federally-assisted housing, will be assured of long-term (20 years) commitment of Section 8 rent subsidies, including Mark-Up-to-Markets vouchers, to satisfy underwriters, including ELIHPA and original HAP contracts.

At the present time, there is a Catch–22 with underwriters wanting long-term commitment for rent subsidy; yet counter-productive with current budget scoring system discouraging long-term commitments. AAHSA recommends that the Committee collaborate with the Budget Committee and other appropriate agencies to change existing budget scoring requirements to accommodate long-term commitment

of rent subsidy funds without front-loading budget requirements. AAHSA also recommends that fund be earmarked for not-for-profit preservation efforts with the establishment of a national housing trust fund, and/or encouraged preservation funds for State or local housing trust funds.

Modernization Grants for Nonprofit Sponsored Elderly Housing

AAHSA recommends that a specific line-item program be established to provide modernization and rehabilitation grants for qualified not-for-profit sponsored affordable elderly housing. These funds would complement the use of recaptured IRP funds targeted for modernization/rehabilitation of nonprofit sponsored Federally-assisted elderly housing. These funds could be used for rehabilitation, retrofitting, and modernization, including conversion of efficiencies into one-bedroom apartments, community space, and/or other uses to improve the quality of life of older residents and financial soundness of the facility. AAHSA supported similar language that was enacted earlier, and supports provisions included in H.R. 3995. AAHSA recommends that HUD be instructed to implement promptly this program and that Congress provide specific modernization funds for this purpose.

HUD Guidelines on Section 202 Refinancing and Limited Partnership

AAHSA recommends that HUD be instructed to expedite compliance with Congressional intent to enable owner options with refinancing Section 202's, including clear guidance that "once a Section 202" always considered as a Section 202 for purposes of option to participate in legislative or administrative actions earmarked for nonprofit sponsors of Federally-assisted housing. In addition, AAHSA recommends that multifacility owners have the option to combine the refinancing of Federally-assisted properties within their portfolio, including statewide, regional, or other economic groups; and have the option to pool the savings from refinancing all or portions of their portfolio, as well as access to pooled residual receipts and reserve accounts, for purposes of refinancing, enhancing services, expanding supply or other benefits to preserve or expand the supply of affordable housing for older persons. With this increased flexibility, the multifacility sponsor will ensure that the resources pooled among the facilities will be available for each of the specific projects within the pool, as needed. AAHSA recommends that not-for-profit organizations be entitled to developer fees and distribution rates similar to the level provided by State housing finance agencies for refinancing Federally-assisted housing projects.

Transition and Preservation Vouchers

AAHSA recommends that transition vouchers be provided for existing residents that choose to remain in their facility that is being converted to market rate (similar to enhanced vouchers). However, for each affordable housing unit that is converted to market rate we recommend that a companion Preservation Voucher be provided for nonprofits to develop replacement long-term affordable housing in that local community, State, or region. In addition, we would recommend that special project-base vouchers be established to accompany the transfer of the ownership to qualified nonprofit preservation entities.

Conclusion

In closing, I would like to express again our appreciation for the leadership that the Committee is taking to preserve affordable housing in this country. We have serious concerns that critically needed affordable housing is gradually being lost, culminating in a "silent crisis"—below the radar screen of the general public and policymakers. We would hope that these hearings will serve as a wake-up call to this looming crisis. Some of the gradual loss of affordable housing may be due to unintended consequences of enhanced vouchers which have tended to numb or neutralize outcries from existing residents as their unit is converted to market rate. As stated earlier, we believe that enhanced vouchers only provide a short-term solution for existing residents and tend to mask, hide the need for affordable housing for the scores of low-income seniors on multiyear waiting lists and for the future waves of older persons, including aging baby-boomers who will be turning 65 in less than a decade.

In addition, some of the gradual decline in affordable housing may be due to a lack of consistency with both production and preservation strategies between Congressional intent and implementation by the Administration. Some of the loss may also be attributed to simply HUD and other agencies being understaffed and/or with inexperienced staff that have misunderstood Congressional intent. Finally, some of the loss of Federally-assisted housing may be attributed to a gradual devolution of housing from the Federal Government to State and local governments and to the private sector; as well as market forces and other factors.

Some of the recommended solutions to halt the loss of affordable housing are beyond the jurisdiction of this Subcommittee. These include: Revisions to exit and other tax policies; the need to improve HUD–HHS collaboration to "preserve" existing elderly housing facilities by adapting the facility to accommodate services and health care; and even budget scoring constraints, such as long-term commitments for Section 8 or other rent subsidies; and budget scoring with debt forgiveness of the existing Federal Section 202 mortgage. Therefore, we would urge that the Subcommittee seek collaborative solutions with other committees and agencies to address preservation needs. The Subcommittee may want to conduct an Interagency Task Force to examine cross-cutting preservation issues.

We are pleased to contribute to your deliberation on these critical issues, and we urge your support for the recommendations outlined in our testimony.

For additional information on this testimony, please contact Larry McNickle *lmcnickle @aahsa.org*.

Four Phases of Section 202 Elderly Housing Assistance

(Highlights -- chart does not show all administratively important changes occurring within each phase.)

	Original Section 202	Sec 202 with Sec 8		Sec 202 with PRAC
		Pre-"Cost Containment"	With "Cost Containment"	
Years in Effect	1959 - 1973	1975 - 1981	1982 - 1990	1991 - Present
Elderly Housing Produced	335 Projects 45,275 Units	1,996 Projects 125,365 Units	2,821 Projects 88,723 Units	295 Projects 50,128 Units
Program Structure	50 year amortizing loan with interest rates originally subsidized down as low as 3 percent. Later, interest was raised to the federal borrowing cost plus an administrative fee. *For 1973-5, Sec 236 interest subsidies were the only federal elderly housing assistance.*	40 year amortizing loan with interest rates set at the federal cost of borrowing plus a fee to cover administrative costs; 20 year Sec 8 project-based rent assistance attached to each unit. Sec 8 contract rent covers the cost of Sec 202 loan principle and interest payment.	Same loan and rental assistance structure, but "cost containment" (1) severely limited common areas and amenities, (2) forced over-reliance on efficiency units, (3) led to inadequate structural design, (4) created need to retrofit projects to achieve marketability	40 year non-interest bearing capital advance -- non-repayable if the project complies with program Five-year Project Rental Assistance Contract (PRAC) pays sponsor the difference between (1) operating costs of units occupied by very low income, and (2) tenant contribution.
Eligible uses for capital	New construction	New construction, substantial rehabilitation, acquisition with substantial rehab	Same	New construction, reconstruction, or acquisition with moderate or substantial rehab
Income eligibility	None until 1962 then, 90 percent of area median	Below 80 percent of median	Below 50 percent of area median	Below 50 percent of area median target eased for 1995
Resident rent payment	Set by project rent	25 percent of adjusted income	30 percent of adjusted income after 1984	The highest of: (1) 30 percent of adjusted monthly income, (2) 10 percent of income, or (3) housing portion of welfare
Other	Ended by the Nixon moratorium on federal housing programs. In recent years, some projects receive Sec 8 rental assistance to ease financial stress.	1983 Housing Act ended Sec 8 assistance for new construction except for Sec 202 housing.	Properties have a special need for additional capital investment to overcome structural inadequacy.	Service coordinator and up to 15 percent of supportive services and service coordinator are eligible costs under the PRAC.

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Appendix G–3

PRESERVING AND IMPROVING SUBSIDIZED RENTAL HOUSING STOCK SERVING OLDER PERSONS: RESEARCH AND RECOMMENDATIONS FOR THE COMMISSION ON AFFORDABLE HOUSING AND HEALTH CARE FACILITY NEEDS FOR SENIORS IN THE 21ST CENTURY

Michael Bodaken & Kyra Brown

NATIONAL HOUSING TRUST

March 1, 2002

Executive Summary

We live in an aging Nation. This demographic reality is irrefutable. As we proceed through the first decade of the 21th Century, our Nation will be increasingly challenged by problems that confront our current and future elderly households. Safe, accessible, and affordable housing is critical to good health and function at any age. But the relationship between housing and health is, perhaps, more apparent when one is faced with the frailties associated with old age. As we age, more and more health care is provided at our homes. Future demographic drivers call for numerous innovations to meet the affordable housing and supportive services needs of older persons. Much has been written about the *production* of new units to meet these needs. This document, written for the Commission on Affordable Housing and Health Facility Needs for Seniors in the 21st Century focuses on *preserving and improving existing* senior affordable housing.*

While the goal of preservation may be obvious, it is not always clear how this stock should be recapitalized and improved. Affordable senior housing, like its occupants, is undergoing an "aging process." Most of it was developed through private/public partnerships more than two decades ago and much of the stock is itself in need of updating and repair. Not surprisingly, as the average age of the population in this housing has climbed, so have their needs. The dilemma that confronts us is how to both preserve what we have and, simultaneously, meet the changing needs of those who call it home. The goal of this study is threefold:

(1) To provide specific data on the existing subsidized elderly rental housing stock in the United States.

(2) To summarize that data in a comprehensive, easy-to-read format for the Commission on Affordable Housing and Health Facility Needs for Seniors in the 21st Century and the general public. This report will include information on what properties have already been "converted" to market-rate units where the majority of the units are occupied by older persons, the ages and races of the existing occupants, and the number of properties serving primarily the elderly that may be capable of refinancing in the not too distant future.

(3) To make recommendations on how to preserve and to improve existing subsidized elderly homes. Our analysis includes a discussion of new tools approved by HUD to preserve elderly, HUD-insured properties. These include: Prepayment of existing Section 202 loans; the use of 501(c)(3) bonds, private activity bonds, and low-income housing tax credits to revitalize this stock; the possible curtailment of debt in Section 202 properties; and policy recommendations to facilitate the conversion of existing subsidized housing serving mainly the elderly to assisted living facilities.

We begin with a general summary of the various Federal programs that serve the rental housing needs of older persons. In particular, we focus on those programs that have HUD Section 8 or other types of Federal subsidies. The document proceeds to analyze what we have chosen to designate as "primarily elderly" properties, that is, properties where over 50 percent of the households served are older persons, age 62 or over. In our study, we found that in recent years, more than 250 properties that primarily serve the elderly have prepaid their HUD FHA-insured mortgage or opted-out of their Section 8 contracts, in the process releasing over 20,000 apartments from their previously regulated rents. We expect this trend to continue since many properties that primarily serve older persons have high interest rates

*The National Housing Trust wishes to acknowledge the generous and unstinting assistance of the following individuals in the preparation of this document for Commission on Affordable Housing and Health Facility Needs for Seniors in the 21st Century: Andrew Kochera, AARP Public Policy Institute; Don Redfoot, Ph.D., Senior Policy Advisor, AARP; Gary Eisenman, Related Capital Companies; and Michael Reardon, Nixon, Peabody, LLC.

with current rents below market. At the same time, we believe a good case can be made to current and future owners of this housing that their economic interests and preservation of affordable housing can be readily aligned.

Indeed, signs of hope are emerging. New HUD tools are at our disposal to renovate subsidized, senior housing. Additionally, State and local housing finance agencies, increasingly aware of this housing problem, are providing greater resources for its resolution. Some subsidized housing owners are already converting their facilities to assisted living sites to accommodate the changing needs of their tenant profile. In this study, the Trust explains how an owner of primarily elderly, subsidized housing can use some of these tools to rehabilitate the property without raising the occupants' rents. The Commission should encourage these trends and propose other meaningful, cost-efficient programs to save this unique housing resource.

Moreover, our recommendations recognize the devolution of housing programs and resources to State and local governments. As the Commission will see, a great many States are already devoting considerable resources, including low-income housing tax credit set asides, for the preservation of the primarily elderly, subsidized housing stock. However, much more can be done. The data reveals that this problem will grow in the coming decades. The Federal Government still has a strong role to play, including encouraging State and local governments to "steer" their resources toward maintaining this unique housing stock. The adoption of the Affordable Housing Preservation Act of 2001 would be a significant step in that direction.

The recommendations that follow flow directly from the Trust's initial analysis of the data and our belief that the Federal Government cannot abdicate its role to save this housing. No one expects the Federal Government to do this by itself. But the Federal Government can play a significant role by: (1) Setting aside existing resources for preservation; (2) Increasing the flexibility of existing HUD tools for preservation; and (3) fully funding programs that match State and local efforts to preserve primarily elderly, subsidized housing.

Recommendations

RECOMMENDATION NO. 1: Recommend that an ongoing database be established providing project specific information on primarily elderly, subsidized properties that (a) have Section 8 contract rents at or below market and/or, (b) have loans with significantly high current interest rates. These properties arguably have a high risk of mortgage prepayment and should be placed on an "early warning" list to be shared with State Housing Finance Agencies, HUD, the Rural Housing Service, and the general public.

RECOMMENDATION NO. 2: Recommend that State Housing Finance Agencies set aside or prioritize the use of low-income housing tax credits and private activity bonds to preserve and improve affordable, subsidized, primarily elderly housing.

RECOMMENDATION NO. 3: Recommend that Congress strongly encourage HUD to facilitate "Mark-Up-to-Market" Section 8 contract rents for elderly, subsidized properties with current rents below market to prevent Section 8 opt-outs by private owners and permit current nonprofit owners the resources needed to meet their ongoing operating costs. Additionally, it is absolutely critical that nonprofit owners of such properties receive distributions from their properties to meet other mission-related activities.

RECOMMENDATION NO. 4: Recommend that useful information be provided to owners of existing HUD-insured, Section 236 properties primarily serving older persons. The distribution of information should include a simple explanation of how the owner can take advantage of HUD's Section 236 "decoupling process" to rehabilitate the property and keep it affordable.

RECOMMENDATION NO. 5: Recommend Congress urge HUD to immediately establish a program for use of the recaptured Interest Reduction Payments that are now in an IRP Pool at HUD. Furthermore, Congress should urge HUD to use at least a third of these for the preservation and improvement of existing HUD-insured, Section 236 properties primarily serving older persons.

RECOMMENDATION NO. 6: Recommend Congress urge HUD to permit subordination of its Section 202 mortgage to new debt brought in with tax credits where the new debt and tax credits actually enhance the property's value and livability.

RECOMMENDATION NO. 7: Recommend Congress encourage HUD to prepare a report to explain to Section 202 owners the comparative costs and benefits of prepaying its current loan with 501(c)(3) bonds or refinance with new debt and low-income housing tax credits.

RECOMMENDATION NO. 8: Recommend that Congress revisit the issue of waiving all or part of the existing debt on Section 202 properties supported by Section 8.

RECOMMENDATION NO. 9: Recommend that Congress fund a meaningful study of how to best facilitate conversion, where appropriate, of existing subsidized housing

to assisted living facilities. This study should document the costs of such conversion, and in particular, conduct a cost/benefit analysis of such conversion. The study should determine whether conversion to assisted living prevents premature institutionalization, and it should ask practitioners to provide detailed training on how to efficiently undertake these conversions. Congress should allow industry practitioners and others to provide detailed testimony on the recent Senate bill 1886, the "Assisted Living Tax Credit Act," introduced by Senator Dodd (D–CT), which allows for a business credit for supported elderly housing.

RECOMMENDATION NO. 10: The Commission should urge Congress to immediately consider, amend, and adopt Senate bill 1365, the Affordable Housing Preservation Act of 2001. *The Commission should urge Congress to amend the Senate bill 1365 to include Section 202 housing as eligible for grants provided pursuant to the Act.* Further, the Commission should recommend that at least $300 million of funds should be devoted to the Affordable Housing Preservation Act of 2001 and that no less than a third of these funds should be devoted to the preservation and improvement of primarily elderly, subsidized housing.

Narrative

The Need to Preserve and Improve Affordable Rental Housing for Older Persons

We live in an aging Nation. The demographics are irrefutable:

- Growth in senior households (ages 65 and older) will surge in the coming decades. By 2030, the senior population will double to nearly 70 million, bringing their share of the total U.S. population to 20 percent. The number of those aged 85 and older will nearly quadruple, going from 3.5 million to 14 million by 2030.[1]
- Further, almost a third of the growth between now and 2010 of one-person households will be for those over age 65.[2]
- Assisted communities are home to only 3 percent of the Nation's senior population.[3] Nevertheless, as elderly households age in place, the need for future *affordable* assisted living increases. The possibility of converting elderly, subsidized dwellings to assisted living facilities is just now being explored.
- 4.6 million elderly households are renters; almost a third of these households—1.5 million—pay more than 50 percent of their incomes for rent and/or are living in substandard housing.
- The median net worth of elderly rental households is less than $7,000 compared with the median net worth of $141,000 for elderly homeowners.[4]
- Older renters in subsidized housing are two to three times as likely to report disabilities than older homeowners.[5]
- Wealth and income disparities will widen, limiting the housing choice of poor elderly households: "[t]he sharp disparity in wealth among baby boomers will carry well into their retirement years, leaving many lower-income seniors with few housing and special care options. Elderly renters will face particularly onerous housing cost burdens."[6]
- The number of older persons residing in subsidized housing (over 1.9 million) is greater than the number of persons residing in our Nation's nursing homes.[7]
- In recent years, nearly 900,000 unsubsidized, affordable housing units have been lost from the affordable housing stock due to demolition or rising rents; an additional 150,000 subsidized units have been converted to market-rate housing.[8] Most subsidized senior housing facilities have long waiting lists. For instance, the AARP study of Section 202 facilities shows there is a nationwide average of nine older applicants for every vacant Section 202 apartment that becomes available each year. A similar waiting list confronts those who are in line for a low-income housing tax credit unit.[9]

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[1] Joint Center for Housing Studies of Harvard University, *Housing for Seniors,* 2001.

[2] Joint Center for Housing Studies of Harvard University, *The State of the Nation's Housing: 2001,* p. 10.

[3] Ibid.

[4] Ibid.

[5] AARP Public Policy Institute, *Adding Assisted Living to Subsidized Housing: Serving Frail Persons with Low Incomes,* Wilden and Redfoot, January 2002.

[6] *Housing for Seniors,* 2001.

[7] National Center for Health Statistics, 2000 and data derived from AARP study, January 2002.

[8] Compilation of data from National Housing Trust and the Joint Center for Housing Studies' *The State of the Nation's Housing: 2001.*

[9] "Serving the Affordable Housing Needs of Older Low-Income Renters: A Survey of Low-Income Housing Tax Credit Properties" (Executive Summary), Andrew Kochera, AARP Public Policy Institute, January 2002.

Types of Existing Subsidized Rental Housing Primarily Occupied by Older Persons

Over the past 40 years, the Federal Government has, through a private/public partnership, produced more than 800,000 apartments specifically designed to provide decent, safe, and affordable homes to poorer, older persons. This apartment inventory constitutes the most significant source of affordable housing for our Nation's elderly population. The following describes the programs that produced this important housing resource.

Section 221(d)(3) BMIR and Section 236

The Housing Act of 1961 authorized the Section 221(d)(3) below-market interest rate (BMIR) program. The program insured 40-year mortgages made directly to nonprofit and limited dividend sponsors. Typically, the interest rate was 3 percent. The Housing and Urban Development Act of 1968 added Section 236 to the National Housing Act, which combined 40-year mortgage insurance with subsidized interest payments to the lender for the production of low-cost housing. The interest rate subsidy lowered the effective rate to the owner to 1 percent. Eventually, many of these projects received additional project-based Section 8 assistance to provide additional rental assistance payments to owners on behalf of very-low income (50 percent median-income or less) tenants.[10] Nearly 1 million apartments were produced under the Section 221(d)(3) BMIR and Section 236 programs. Under both programs, the owner had the "right to prepay" the mortgage after 20 years and end the affordability restrictions.

Some of the Section 236 projects are nonprofit sponsored developments specifically designed for older persons. Indeed, a flurry of these Section "236/202" elderly developments occurred between 1969 and 1976, in large part due to the moratorium on construction of elderly Section 202 properties between 1969 and 1976.

According to data analyzed by the National Housing Trust for the Commission, 657 properties with 91,956 Section 221(d)(3) BMIR and Section 236 affordable, subsidized apartments are primarily (50 percent or more households in property are 62 or older) elderly properties. Many more elderly households—163,958 households according to HUD data—reside in 221(d)(3) BMIR and Section 236 apartments in properties that are not primarily elderly.[11]

Section 202 Program

Congress enacted the Section 202 elderly housing program in the Housing Act of 1959. The Section 202 program has been successful, producing more than 320,000 apartments, of which approximately 170,000 are also assisted with the Section 8 housing subsidies. Since 1959, the Section 202 program has gone through three basic program structural changes. The recent Affordable Housing for Seniors and Families Act has initiated a fourth basic structural change in the program.

Initial Program Structure

When enacted in 1959, the Section 202 program provided direct loans from the Federal Government to eligible nonprofit entities. Originally, the loans were typically for a 40-year term at a 3 percent interest rate, although later HUD determined the interest rate based on the cost of Government borrowing. The loans could be used to cover the costs of new construction or substantial rehabilitation of rental housing for the elderly and the handicapped and the loans could not be repaid without the approval of the Government. The requirements for the operation of the projects were embodied in a Regulatory Agreement that controlled the rent levels to ensure project affordability. However, there was no rental assistance provided to the project owners. Tenant rents were set at the level necessary to cover the cost of repaying the loans and project operations. While much of this stock is in decent physical condition, there has not been sufficient income to allow for major capital improvements.

Introduction of Section 8 Rental Assistance

As the cost of Government borrowing increased, the interest rates on Section 202 elderly housing projects rose, making it more difficult to maintain affordability in the projects. In 1975, HUD was authorized to provide Section 8 assistance to Section

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[10] Generally rental assistance from the Federal Government covers the difference between what the tenant is obligated to contribute toward rent—typically 30 percent of his/her income—and the rent charged by the landlord. Because tenants' incomes are so low, their payment often does not pay the operating cost of the property. At least 13,686 project-based properties, containing 914,847 Section 8-assisted apartments, will have their Section 8 contracts expire during the next 5 years.

[11] U.S. Department of Housing and Urban Development, Office of Policy Development and Research, *A Picture of Subsidized Households in 1998,* August 1998.

202 elderly housing projects. Between 1975 and 1990, HUD provided direct loans to eligible nonprofit borrowers under a 40-year note and mortgage. Simultaneously, HUD provided properties with 20-year Section 8 project-based rental assistance contracts. With the exception of projects that closed between approximately 1977 and 1981, the notes and mortgages on these projects cannot be prepaid without the approval of HUD. Operations of these projects are governed by a Section 202 Regulatory Agreement and Section 8 housing assistance payments contract. Today, the Section 8 contracts are renewed on an annual basis at rents that are the lesser of the existing rent multiplied by the applicable operating cost adjustment factor (OCAF) published by HUD or at a budget-based rent.

Capital Advance Program

In the National Affordable Housing Act of 1990, Congress significantly altered the structure of the Section 202 elderly housing program. First, Congress provided for two separate and distinct programs for older persons and for persons with disabilities. New construction under the Section 202 program is now exclusively for older persons—defined by HUD as persons 62 years of age and older. Second, Congress changed the program from a loan program to a capital advance program. Under the capital advance program, HUD basically provides a grant to the project that the owner is not required to prepay unless the owner does not operate the project in accordance with the program requirements for the 40-year term of the capital advance. HUD has structured the program so that the obligation of the owner to operate the project in accordance with the Section 202 program requirements is secured by a zero-interest, 40-year note and mortgage, which is not required to be repaid unless the owner is in default. Third, Congress decided that the rental assistance received by Section 202 projects would no longer be provided through the Section 8 housing assistance payments program. Instead, HUD provides a renewable rental assistance contract (PRAC) to Section 202 projects. The operation of the PRAC is essentially the same as the Section 8 housing assistance program, but the appropriations for the rental assistance are provided under the Section 202 program and not under the Section 8 program.

Affordable Housing for Seniors and Families Act

In December of 2000, Congress again made significant changes to the structure of the Section 202 program. First, Congress amended the Act to provide for a change in the nature of eligible ownership entities. Over the years, one of the constants in the Section 202 elderly housing program was the requirement that the project be owned by a nonprofit entity. In the new legislation, Congress amended the eligible owner definition of "private nonprofit organization" to include for-profit limited partnerships, in which the sole general partner is an organization that qualifies as a private nonprofit organization, or corporations that are wholly-owned and controlled by a private nonprofit organization. Through this amendment, Congress intends to bring to the Section 202 program additional funding sources that have previously not been available to these projects, including most particularly the possible use of low-income housing tax credits. Second, Congress enacted legislation that requires HUD to approve the prepayment of Section 202 loans with a prepayment plan under which (i) the owner agrees to operate the project under terms at least as advantageous to tenants as required under the original Section 202 program terms or the Section 8 housing assistance payments contract and (ii) the prepayment may involve refinancing of the loan if the refinancing results in a lower interest rate and reductions of debt service. At least 50 percent of any Section 8 savings resulting from the refinancing shall be made available to the owner for purposes such as increased supportive services, rehabilitation or retrofitting of buildings and units, or the construction of additional facilities for the project which could include facilities such as additional community space or assisted living facilities.

In addition to providing the owner savings resulting from a refinancing, the new law contains other provisions that may be used in the prepayment and refinancing plan, including:

- The law requires the Secretary to make available to the owner funds in the project's residual receipts account (these accounts accrue when the annual income to the owner from tenant payments and HUD rental assistance payments are more than are needed to meet project debt service and operating expenses) and the reserve for replacement accounts. The residual receipts account must be maintained at a minimum of $500 per unit and the reserve for replacement account must be maintained at a minimum of $1,000 per unit.

NATIONAL HOUSING TRUST

All Mortgage Prepayments by State

State	Properties	Total Units
Alabama	2	212
Alaska	4	368
Arizona	13	1,341
Arkansas	4	402
California	283	29,883
Colorado	23	2,299
Connecticut	16	1,999
Delaware	2	191
District of Columbia	8	561
Florida	25	3,244
Georgia	19	2,121
Hawaii	4	834
Idaho	5	228
Illinois	17	2,269
Indiana	29	4,074
Iowa	9	675
Kansas	3	309
Kentucky	8	832
Louisiana	9	807
Maine	3	504
Maryland	24	3,876
Massachusetts	44	5,732
Michigan	21	3,698
Minnesota	14	1,585
Mississippi	3	378
Missouri	14	1,093
Montana	6	305
Nebraska	4	503
Nevada	7	754
New Hampshire	7	671
New Jersey	11	1,116
New Mexico	8	1,032
New York	12	1,813
North Carolina	20	2,485
North Dakota	3	88
Ohio	29	2,695
Oklahoma	2	412
Oregon	35	1,531
Pennsylvania	12	2,283
Puerto Rico	1	298
Rhode Island	2	354
South Carolina	22	2,209
South Dakota	2	150
Tennessee	8	1,014
Texas	67	11,566
Utah	10	447
Virginia	37	5,966
Washington	26	1,691
West Virginia	1	64
Wisconsin	14	1,158
Wyoming	1	12
TOTAL	**953**	**110,132**

Data compiled from several HUD sources and not independently verified.

National Housing Trust, 2002.

All Section 8 Opt Outs by State

State	Properties	Contracts	Assisted Units	Total Units
Alabama	11	11	365	1,114
Arizona	4	4	335	649
Arkansas	11	12	436	889
California	135	140	8,162	12,326
Colorado	14	19	1,011	1,617
Connecticut	16	18	821	1,293
Delaware	2	3	100	248
District of Columbia	11	12	246	645
Florida	14	16	1,040	1,808
Georgia	10	10	528	1,114
Hawaii	2	3	91	91
Idaho	7	7	129	409
Illinois	33	38	1,807	3,698
Indiana	31	36	1,302	3,458
Iowa	36	36	1,290	1,296
Kansas	15	16	469	1,410
Kentucky	11	12	342	648
Louisiana	10	10	666	1,799
Maine	1	1	32	32
Maryland	21	22	1,087	2,824
Massachusetts	9	10	511	1,521
Michigan	37	45	1,852	5,900
Minnesota	4	5	63	254
Mississippi	6	7	317	460
Missouri	27	31	941	1,648
Montana	8	8	247	452
Nebraska	4	4	100	181
Nevada	7	8	349	1,146
New Hampshire	8	8	324	568
New Jersey	4	4	214	218
New Mexico	4	4	218	392
New York	24	26	2,176	2,887
North Carolina	22	23	790	2,158
North Dakota	12	12	280	311
Northern Mariana Islands	2	2	45	45
Ohio	128	137	5,703	6,791
Oklahoma	4	7	67	249
Oregon	17	18	481	587
Pennsylvania	10	11	676	1,043
Puerto Rico	6	6	572	851
Rhode Island	12	15	436	483
South Carolina	15	17	498	1,686
South Dakota	7	9	146	194
Tennessee	16	18	461	1,533
Texas	85	113	5,707	12,088
Utah	6	7	150	476
Vermont	1	1	15	60
Virginia	14	16	1,027	1,684
Washington	33	41	1,291	2,330
West Virginia	1	1	20	200
Wisconsin	22	22	709	1,210
Wyoming	3	5	168	169
TOTAL	**953**	**1,067**	**46,813**	**87,143**

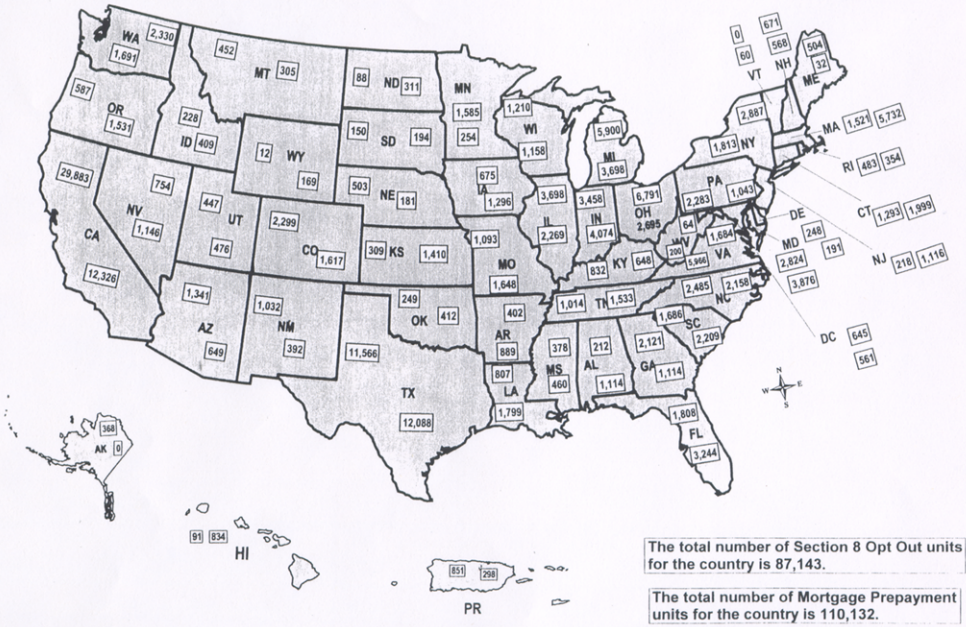
Data compiled from several HUD sources and not independently verified.

National Housing Trust, 2002.

Section 8 Opt Outs and Mortgage Prepayments by State

The number of Section 8 Opt Out units are in BLUE

The number of Mortgage Prepayment units are in RED



The total number of Section 8 Opt Out units for the country is 87,143.

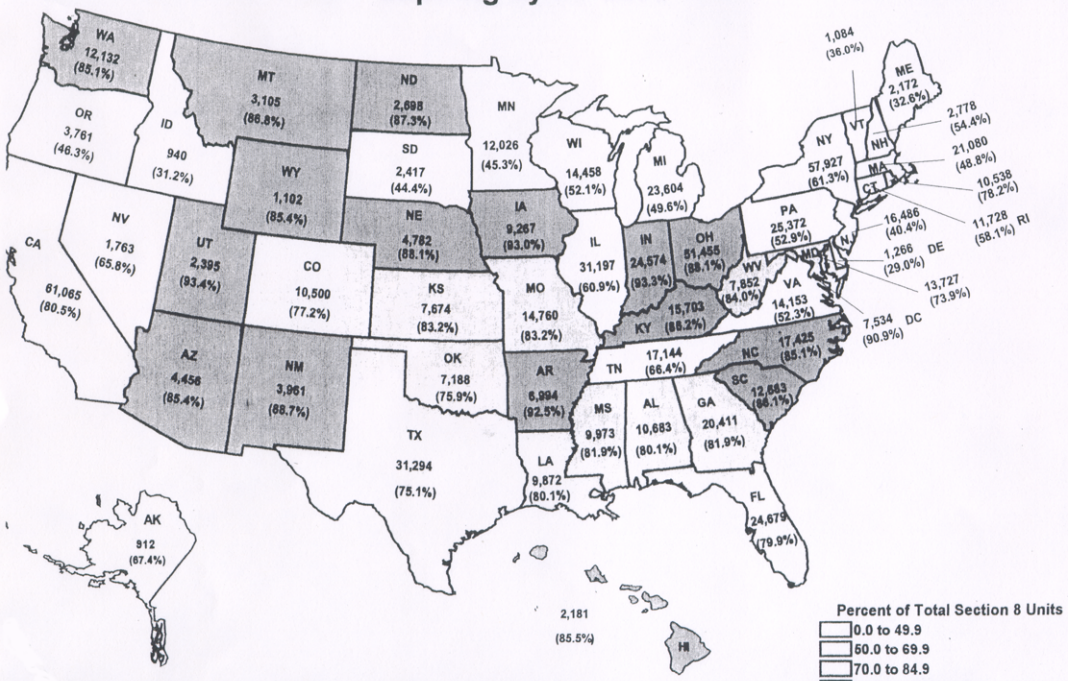
The total number of Mortgage Prepayment units for the country is 110,132.

Total Number of Opt Outs and Prepayments: 197,275

Data Source: Compiled from data supplied by the National Housing Trust.

Map created by Community Maps, Inc. on April 22, 2002.

Number of Project-Based Section 8 Units Expiring by FY 2005



Expiring units as a percent of project-based Section 8 units in the state in parenthesis.

Data compiled from several HUD sources and not independently verified. Does not include 202/811 properties
(Data current as of March 2002)

National Housing Trust, 2002.

PREPARED STATEMENT OF LOUISE SANCHEZ

PRESIDENT, NATIONAL ALLIANCE OF HUD TENANTS, NEW YORK, NEW YORK

OCTOBER 9, 2002

On behalf of the National Alliance of HUD Tenants (NAHT), we are pleased to submit these comments regarding preservation of the Nation's privately-owned, subsidized housing stock. As you know, NAHT has sought such a hearing for several months, as reports emerged of the alarming erosion of the Nation's affordable housing due to unregulated owner decisions to opt-out of Federal subsidy programs. We want to thank you, Senator Reed, for your leadership in calling this hearing, and appreciate the opportunity to testify today.

Founded in 1991, *the National Alliance of HUD Tenants (NAHT) is the Nation's only membership organization representing the 2.1 million families who live in privately-owned, HUD-assisted housing. Our membership today includes voting member tenant groups and 45 areawide tenant coalitions or organizing projects in 30 States and the District of Columbia.* We are governed by an all-tenant Board of Directors elected by member organizations from all 10 of HUD's administrative regions at our annual June Conference. I have served as NAHT Board President for the past year, and have been a NAHT Board member since 1997. I also serve as the Co-Chair of the Mitchell-Lama Residents Coalition, which represents over 101,000 families in Mitchell-Lama subsidized developments in New York State. I am also President of the Michelangelo Tenants Association, a 440-unit HUD-subsidized Mitchell-Lama development where I live in the Bronx.

As the first national tenant union in the United States, NAHT has joined the International Union of Tenants (IUT), which named October 7 as International Tenant Day to coincide with World Habitat Day declared by the United Nations, in which the IUT has consultative NGO status. We appreciate that the timing of today's hearing has helped to honor the growing movement to meet the world's housing needs.

The Nation is Losing Affordable Housing at an Alarming Rate

This past weekend, the NAHT affiliates in several cities released a new report documenting the dramatic loss of affordable housing in America since 1996, when the United States pledged to do more, not less, to meet the Nation's housing needs at the UN Habitat II Conference in Istanbul. Instead, our report shows *that the United States has lost more than 250,000 units of affordable housing since 1996,* following Congress' restoration of owner's ability to "prepay" (for example, pay off after 20 years) their 40-year HUD-subsidized mortgages and raise rents to high market levels. Of this amount, *a total of 199,764 units of privately-owned HUD-subsidized housing was lost to owner decisions to prepay or to "opt-out" of expiring project-based Section 8 contracts as of August 2001.* The remaining units lost consist of the net loss of Public Housing through HOPE VI demolitions. We are submitting a copy of this report* with my testimony today, which includes data on prepayments and opt-outs by State.

The NAHT was the only national organization to speak out against repeal of the regulatory structure of the Title VI Preservation Program in 1996, which provided additional HUD subsidies to owners in exchange for guaranteed repairs, permanent affordability, and the promotion of transfers to nonprofit and tenant ownership. We warned of dire consequences for the Nation's affordable housing stock if this regulatory program were repealed. Unfortunately, the data show that these predictions have come true.

Mark-Up-to-Market Has Not Been Enough

When press reports of tenant displacement spurred Congress and HUD to act in 1999 to stem the losses, many observers thought that the problem was "solved" through adoption of the Mark-Up-to-Market Program, whereby HUD offers generous increases in Section 8 subsidies to owners who voluntarily agree to maintain affordability for 5 to 20 years. In our report, we compare the number of units lost through prepayment and opt-out in the 2½-year period from 1996 to early 1999, when Mark-Up-to-Market was adopted, with the equivalent 2½-year period through August 2001, using data compiled by the National Housing Trust from several HUD sources.

These data show that, *despite Mark-Up-to-Market, the average annual loss of housing nationally has remained roughly the same as before its adoption—about 41,000 units continue to be lost each year.* While no doubt this figure would have

*Held in Committee files.

been even higher without Mark-Up-to-Market, clearly, we need to do more to preserve the Nation's affordable housing stock.

Some States are Particularly Hard Hit

Looking at the data for each State, it is clear that the loss of affordable housing is a truly national problem. But some areas have been particularly hard hit. *By August 2001, California and Texas alone had lost 65,863 units of privately-owned affordable housing, nearly a third of the national total lost.*

A number of States have actually experienced a dramatic increase in the rate of loss, despite the adoption of Mark-Up-to-Market. *Overall, 14 States, including Missouri, Indiana, and South Carolina, have seen an increase in the rate of at least one category of units lost by more than 300 percent since early 1999. Likewise, a number of smaller and more rural States such as Iowa, Nebraska, New Hampshire, and Montana* where HUD-subsidized housing represents a relatively large portion of the State's affordable housing and often the only affordable housing available in sparsely populated areas, *have experienced a rapid rise in units lost.* Some other large States, such as Pennsylvania, Ohio, and Georgia, have also experienced a significant increase in the rate of loss.

Housing Crisis in New York City

Most startling of all, however, is the new data we are releasing today regarding New York City, where I live. Our report includes a chart prepared by the Mitchell-Lama Residents Coalition, which I serve as Co-Chair. The Mitchell-Lama program is a resource unique to New York, where the State developed more than 101,000 units of mixed-income, affordable housing using a variety of subsidy tools, including HUD mortgage insurance and subsidies under the Section 236, RAP, and Section 8 programs. As in other States, owners of Mitchell-Lama buildings are now eligible to "prepay" or "buyout" their Government-subsidized mortgages.

The results are shocking. We have already lost 3,151 units through prepayment, and owners of another 5,767 units in 11 developments have filed Notices of Intent to Prepay with HUD and the State. In addition, four co-ops housing 25,585 families, including the 15,378 unit Co-op City development, are planning to "privatize," prepay their mortgages, and convert to high market rates in the next year. *All told, we have lost or expect to lose 34,503 units of Mitchell-Lama housing in New York City by the end of next year.*

Nor are these the only affordable housing units at-risk in our city. *Another 4,965 units in HUD-subsidized, non-Mitchell-Lama buildings have been lost in New York City since 1996.* An unknown number of these buildings remain at-risk throughout the city.

In the wake of the traumas inflicted on New York City in the past year, the imminent loss of more than 40,000 affordable housing units is a crisis which we can neither bear nor ignore. The people of our city are still reeling from the after shocks of September 11. Mitchell-Lama housing in particular is home to many of the police, firefighters, and health service workers who performed heroically after the September 11 attacks, as well as many low-income and elderly people who simply have no options in the high rental market of New York City.

Homeland security begins with a home. Action by Congress is urgently needed to give us the tools to preserve these affordable units.

Congress Should Adopt a New Regulatory Program to Save At-Risk Housing

It is now clear that voluntary incentives, such as the Mark-Up-to-Market Program, are insufficient to deter owners who choose to opt-out of HUD's contracts in high market areas. NAHT believes that Congress should establish a national regulatory framework to limit owners' ability to opt-out and prepay. For example, restoring the regulatory framework of the Title VI Preservation Program and extending its concepts to expiring Section 8 contracts would preserve more units and be cheaper in the long run than replacing lost units with new construction.

Ironically, in buildings where HUD is executing 5- to 20-year Mark-Up-to-Market contracts, *the cost of additional annual Section 8 Budget Authority and outlays is approaching, and possibly exceeding, the cost of the Title VI Preservation Program, but with none of the benefits.* Although Congress repealed Title VI due to concerns about costs, at least residents and HUD negotiated major repair programs, permanent affordability, and transfers to nonprofit purchasers in 30,000 units.

The equivalent expenditures of Mark-Up-to-Market yield none of these offsetting benefits—in fact, short-term extensions of 5 years leave the residents and HUD at continued risk that owners will opt-out down the road. As long as owners have an unrestricted choice to opt-out of HUD programs, they will be able to leverage ever-

increasing subsidy commitments from HUD—which residents and communities will doubtless support—since the alternative of losing affordable housing is unacceptable. *The restoration of a Title VI regulatory program will, in fact, likely save money,* since mandatory negotiations will lessen owner windfalls and ensure that Congress receives guaranteed benefits on its investment. Substituting capital grant funds for ever-increasing Section 8 contracts, in this context, will likewise achieve savings while preserving housing.

Deregulation is a strategy that has failed in the energy, telecommunications, banking, and airline industries in the United States and in countries around the globe. *The evidence is in—deregulation is a failure in the subsidized housing industry as well.* Congress should act now to restore regulations to save our homes.

HUD Policies Have Contributed to the Loss of Housing

While Congress must provide the funds and regulatory tools to save affordable housing, HUD needs to do more to preserve at-risk buildings. In fact, the record shows that in a number of ways, *HUD policies have added to the loss of housing, rather than its preservation.*

Nowhere has HUD's failure been more dramatic than in the Agency's policies on Property Disposition and Foreclosure for "troubled" HUD housing. In March 2000, the Senate VA/HUD Appropriations Subcommittee held hearings on the loss of affordable housing stock through *HUD's policy of dumping properties it owns or controls for sale on the open market, with only Section 8 vouchers for tenants, no screening of new owners and toothless use restrictions. According to the Subcommittee, more than 26,000 units of formerly project-based Section 8 affordable housing had been sold off in this fashion*—a significant portion of the 86,402 project-based Section 8 "opt-out" units listed in our report as lost between 1996 and August 2001.

To this day, HUD has not collected any data on what happened to the former occupants, or to check on building conditions, rents, and incomes of current occupants, or the effectiveness of HUD's use restrictions. In the absence of any attempt by HUD to monitor or enforce these use restrictions or any data to the contrary, it is reasonable to assume that many of these units no longer serve as housing for the poor, especially in higher market areas. *The Subcommittee should require HUD to investigate and report annually on these questions, as Congress required in its 1994 Property Disposition amendments, but HUD has never done.*

NAHT's member organizations and affiliates in Texas, New Jersey, California, Pennsylvania, and Colorado have challenged HUD's "dumping" policies in a number of Property Disposition cases. In addition, NAHT has challenged other HUD policies which have added to the needless loss of housing, such as the rubber-stamping of mortgage prepayments where HUD approval is required, and HUD's failure to enforce its own rules where owners violate Federal or State laws regarding Notices to Opt-Out or Prepay to tenants or local governments. Since 1997, NAHT has also recommended to HUD that it adopt policies explicitly maximizing the preservation of affordable housing where HUD has discretion to do so. There has been little response by HUD to date.

The testimony submitted today by the National Housing Law Project details several of these policies, and the campaigns waged by NAHT member organizations to save affordable housing in these cases. In the interests of time, we will highlight today a few cases where immediate intervention by the Subcommittee may yet save at-risk buildings affected by these HUD policies of neglect:

BRICK TOWERS (NEWARK, NEW JERSEY). Last week, HUD reportedly "closed" on a sale to the Newark Housing Authority of this 324-unit high-rise building, where residents have been fighting for years to save their homes. In this case, HUD failed to exercise its discretion to negotiate with a nonprofit Joint Venture formed by residents with a reputable developer to save the building with local subsidies, at no cost to HUD. Instead, HUD is providing a $12 million grant to the Housing Authority to demolish the building, with no guarantee of replacement housing. *So HUD is spending $12 million to destroy housing which it could save for nothing. HUD should use its remaining leverage with the Housing Authority to arrange three-way negotiations with the tenant-endorsed Joint Venture to keep the developer's resources and HUD's grant in the city, while saving Brick Towers as part of the deal.*

RAP UP II–B (BOSTON, MASSACHUSETTS). In this 51-unit building in Boston, HUD is poised to sign off on a mortgage prepayment by a defunct "nonprofit" whose Board President/Property Manager was caught "equity skimming" by HUD's Inspector General in 1996, and who is selling the building to new owners who plan to keep him on as manager and convert the buildings to condominiums when HUD's Section 8 contracts expire in 2 years. HUD's Enforcement Center is prepared to look the other way as long as the $110,000 stolen from the property is paid back out of sales proceeds. Instead, *HUD could use its discretion under Section 250 to reject the mort-*

gage prepayment (HUD has no documents establishing that there is a 20-year prepayment option), not approve transfer of the Section 8 contract, and not accept payment for or sign-off on audit findings unless the owner sells to a legitimate nonprofit organization pledged to preserve affordable housing and bar former equity-skimmers from management of HUD's Section 8 contracts. *If the owner fails to comply, HUD should exercise its foreclosure option to preserve affordable housing.*

EAST LIBERTY PROPERTIES (PITTSBURGH, PENNSYLVANIA). A broadly supported nonprofit purchase and redevelopment plan for three troubled housing developments is threatened by HUD's refusal to allow the transfer of existing project-based Section 8 contracts to newly developed replacement housing, even though HUD clearly has authority to do so. *HUD should approve this request forthwith.*

LOS ANGELES SECTION 8 OPT-OUTS. Several owners in Los Angeles have recently attempted to opt-out of expiring Section 8 contracts in violation of State law in California, which requires a 2-year Notice before they can do so. The Los Angeles HUD Office has refused to apply HUD's own Section 8 Policy Guide, which stipulates that HUD staff will certify compliance with State and local laws before signing off on opt-outs or prepayments. The city of Los Angeles has intervened, and tenants are now winning Section 8 contract extensions in court, with no help from HUD. *HUD could still help by requiring owners in the city to restart the Notice process to comply with State law, as required by HUD's Guide.*

HEDCO PROPERTIES (RHODE ISLAND). These consist of three properties totaling approximately 200 units where, as in California, HUD ignored a State law requiring 2-year Notice before prepayment can occur. Tenants sued in State court, which upheld the State law and blocked prepayment. However, last week tenants learned that HUD had sold the HUD-held mortgages on August 28, 2002, to a bank in Plano, Texas, as part of an auction of an unknown number of HUD-held mortgages nationally. HUD's attorneys are now arguing that the mortgage sale has nullified the Regulatory Agreements on these properties, so that the owners are now free to prepay, thus mooting the State court decision. Although details are scarce, including the legal rationale for HUD's position, this is a HUD policy with potentially far-reaching impact on the Nation's housing stock. *We urge the Subcommittee to explore this issue with HUD, determine the extent of the damage, and correct it if possible.*

HUD Appears Unwilling to Enforce the Law

As the Los Angeles and Rhode Island examples illustrate, the problem goes beyond HUD's unwillingness to use its discretion to preserve housing; HUD appears unwilling to enforce or uphold the law, or to use its enforcement powers to penalize owners who violate its regulations.

Perhaps the clearest example of this is HUD's position on enforcing the "Right to Remain" language adopted by Congress in the enhanced voucher program 2 years ago. Where owners opt-out or prepay, Congress has adopted language saying that tenants "may elect to remain" in their units with enhanced vouchers, which guarantee owners the full market rent for their unit, implying that owners have a duty to accept the vouchers. HUD's Section 8 Policy Guide, published in January 2001, clearly states that owners have the Duty to Accept these vouchers as long as tenants wish to remain, and Congress votes the money each year. However, *the Guide actually states that HUD will not enforce this requirement if owners violate it, forcing tenants to find local legal counsel to enforce the law.*

As a result, tenants in several States, aided by NAHT affiliates and legal aid programs in Minnesota, California, Missouri, Philadelphia, and New York have had to file or threaten to file suit to enforce this statute. Although so far all tenants have prevailed in all these cases, the spectacle of the Federal Government refusing to enforce the law, and leaving it up to poor people to do so, does not engender confidence in HUD.

NAHT has also presented numerous other cases to HUD where owners have failed to follow Federal or State law Notice requirements, to provide enhanced vouchers, or to enforce Right to Organize regulations, with spotty results. These examples are too numerous to describe here, although we would be happy to document these for the Subcommittee if you wish. The problem is deeply institutionalized at HUD, ranging from inadequate and/or poorly trained staff at the field office level, to hostility from HUD's Office of General Counsel on some issues, to a lack of protocols for assessing civil monetary penalties where owners violate the law. NAHT has submitted detailed recommendations to HUD on revisions to Handbook 4350.3, the Occupancy Handbook for Multifamily Housing, to beef up HUD enforcement on these matters. *We would appreciate the Subcommittee's help in securing these changes, and shoring up HUD's willingness and capacity to enforce the law.*

HUD's New Leadership Appears Unable to Provide Resources for Tenant Involvement

Since tenants founded NAHT in 1991, we have sought establish a partnership with HUD, whereby tenants—the people with the strongest stake in the successful operation of HUD housing—serve as the unpaid, volunteer "Eyes and Ears" of HUD in overseeing owners and managers of our buildings. Over the years, we have built up a complex institutional relationship with HUD, including on-going relationships with HUD field offices in some 30 States through NAHT's local affiliates; periodic "Eyes and Ears" meetings at the HUD regional level, between tenants in the region and local and Headquarters HUD staff; plenary meetings during NAHT's Annual Conferences in Washington, DC, with HUD's top leadership; and quarterly meetings with key Headquarters staff and the elected NAHT Board.

Key to this relationship, and the ability of tenants at the local building level to participate meaningfully with HUD, has been HUD's provision of resources to enable tenants to organize and articulate their concerns. In MAHRAA, Congress supported this vision by encouraging tenant participation in decisions affecting their homes, and the provision of "up to $10 million" annually through Section 514 to promote tenant and community participation in Section 8 programs.

Since the advent of the new Administration, however, this vision of cooperation has been turned into a nightmare of bungling and broken promises. Administration "froze" all funding to all Section 514 grantees, including the Corporation for National and Community Service and recipients of Outreach and Training Grants (OTAG's) and Intermediary Technical Assistance Grants (ITAG's), because of bureaucratic bungling by HUD. Only when Congressional hearings secured a commitment from the Secretary did the Department resume processing invoices to small nonprofits—several months after funds had been frozen. *HUD delays, unnecessarily intrusive audits, and constantly changing financial requirements have meant that OTAG agencies which received new contracts in January 2001 have been able to receive reimbursements for program outlays for only 10 of the 22 months since these grants commenced—forcing chronic program layoffs and closures.* In effect, small nonprofit agencies who applied for OTAG funds to help tenants have been punished by the new Administration's incompetence and neglect.

To make matters worse, it now appears that several 2001 OTAG grantees will be punished by HUD's IG for not providing HUD with cost allocation plans and timesheet forms which HUD never asked for, had no procedure for accepting, and provided absolutely no training on, despite NAHT's repeated requests for training and offers to help, starting in March 2001.

Last March, the Secretary promised two Congressional Committees that action would be taken to restart the ITAG and VISTA Volunteer Program in multifamily housing, and to designate the Acting Deputy Assistant Secretary for Multifamily Housing, Fred Tombar, to operate the programs. To date, HUD has failed to deliver on these promises.

For example, to date the ITAG mini-grant remains closed. No applications have been approved or accepted for future grants since October 2001. The contracts for the administering agencies have not been extended. This failure effectively shuts down resources to nonprofit groups seeking to acquire at-risk buildings, and deprives tenant groups and small nonprofits with resources they need to assist tenants in their communities. *The Office of Multifamily Housing has been given neither the authority, staff resources, funding nor program control over Section 514, which remains shut down and unstaffed in the Commissioner's office.*

National HUD Multifamily VISTA Project Remains Stalled

Most devastating to tenants has been HUD's continued failure to restart the national VISTA Volunteer project in HUD housing. Funded by a HUD Interagency Agreement with the Corporation for National and Community Service (CNCS), this highly successful project has served as a leading model and prototype for President Bush's call for national service. *Since 1995, the project has helped to empower tens of thousands of residents in HUD multifamily housing to participate in saving and improving their homes. The project funded an average of 50 VISTA Volunteers assigned through State VISTA Offices to locally-based nonprofit agencies in 25 States.* About 40 percent of the VISTA Volunteers have been themselves HUD tenants, who bring new knowledge and leadership skills to their communities at the end of their year of service. The program cost HUD very little money (an average of $750,000 annually for 50 VISTA's and support) and leveraged an equal amount of resources from CNCS. CNCS Chief Executive Officer, Les Lenkowski, has pledged his support for a 3-year extension of the program.

Despite this record, the project has been frozen since November 2001, when HUD failed to honor its contract with CNCS. The effect on tenants across the Nation has

been absolutely devastating. Since HUD never processed the balance of $600,000 owed to CNCS under a $3 million contract signed in 1998, CNCS had to absorb some $133,000 in VISTA Volunteer payroll costs from other sources to prevent a catastrophic Christmas time layoff of volunteers. As a result, CNCS was forced to "freeze" the program, with VISTA's in the field unable to renew and agencies unable to hire new recruits. *Today, only six VISTA's remain, and their terms will end next month.*

In March, Secretary Martinez and Commissioner Weicher reported to Congress that the VISTA project would be restarted immediately, and that the $600,000 owed to CNCS by HUD was being processed. This turned out not to be true. HUD now says that the "old" Agreement cannot be extended. But *there should be no barrier for HUD to execute a new Interagency Agreement at $1.4 million per year with CNCS to restart the project; in fact, it can be restarted for as little as $700,000. This can be done either from remaining Section 514 funds from fiscal year 2002, or the new $10 million which will be available for Section 514 from fiscal year 2003, pursuant to Congressional authorization in the Mark-to-Market Extender bill passed last fall.*

It is hard to understand why a simple Interagency Agreement with another Federal Agency, for a successful program costing HUD very little money, has proven so difficult for the Commissioner's office to process. *We request the Subcommittee's assistance in securing an immediate jumpstart to this project, on an urgent basis, while there is still time to recruit VISTA Volunteers this fall.*

Top Officials Refuse to Communicate with NAHT

Much of HUD's embarrassment in the on-going Section 514 fiasco could have been avoided had the new leadership team communicated with NAHT. For example, in the one meeting which the NAHT Board has had with the new Secretary and Commissioner Weicher, in October 2001, we tried to explain that there was unlikely to have been any ADA violation at OMHAR or at HUD. Our views were rejected, as were repeated attempts to communicate subsequent to this meeting. Even when the IG report exonerated OMHAR, our extensive knowledge of these programs—which could have saved HUD much embarrassment and grief—has neither been sought out nor heard by anyone in a position to make decisions at HUD.

In fact, *both the Secretary's and the Commissioner's office has refused to answer literally hundreds of phone calls, e-mails, and formal written letters signed by NAHT and its associated membership on this, or any other, issue since October of last year.* (Save for a brief meeting with Commissioner Weicher last December arranged by another organization.) *While NAHT enjoys regular access to and a good relationship with HUD career employees such as Acting DAS Fred Tombar and his staff and has opened a new dialogue with the Director of OMHAR, Hank Williams, it is clear that a number of policy issues are made at a higher level in the Department.* Besides the Section 514 issues, these include the full range of issues discussed today which go to the heart of HUD's Preservation of at-risk housing.

In the 25 years, the NAHT and its leaders have been dealing with HUD, this is by far the least responsive and accessible leadership at the Agency we have ever seen. If tenants and their representatives cannot get a hearing with the key policymakers to raise their concerns about policy and enforcement matters which affect their homes, that sends a message the new Administration doesn't really care. When the Administration is unable to honor contracts and invoices with agencies who work with tenants, forcing constant layoffs, and fails to renew a VISTA Volunteer project which aids tenants, that, too, sends a message. *Far from being treated as partners, this Administration treats tenants as if we were the enemy.*

We ask the Subcommittee's help in helping us reestablish the kind of dialogue and partnership, through regular meetings with the Secretary and the Commissioner, which we have enjoyed with several previous Administrations.

Congress Must Adopt New Legislation to Save Our Homes

Although HUD clearly must do more to preserve affordable housing and to reestablish communication with residents, the continued erosion of affordable housing underscores the need for new legislation to stop the continued loss of 40,000 units affordable housing each year. As many more as one million expiring Section 8 or prepayment-eligible units remain at-risk. In a few years, the Nation will be presented with yet another crisis of "expiring mortgages," as the original 40-year mortgages and regulatory agreements expire on some 450,000 units still regulated by HUD. Congress must act now to address this crisis.

The following legislative recommendations have been adopted by the NAHT Board and membership following extensive discussion and input from tenant groups and local tenant coalitions across the country:

(1) ENACT PRESERVATION GRANTS TO SAVE HOUSING. Congresses' 1999 Mark-Up-to-Market initiative has proven inadequate to stop the loss of housing. We urge Congress to complement this program with one or more strategies to provide capital funds for acquisition and repair of at-risk buildings as a further incentive for owners to stay in the program. Generally, *formulating Federal assistance in the form of capital grants with lower on-going Section 8 outlays (to cover lower debt costs) wherever possible will preserve housing at the least long-term costs to the Government,* since the alternative of higher Section 8 outlays (covering higher debt service) will cost more over time due to continuing higher interest payments. In addition, capital grant funds should not be "scored" as a 100 percent Budget Authority expense, since there will be net savings to the Section 8 Certificate Fund in a prepayment building which is "preserved" with capital grant assistance, where enhanced vouchers need not be provided as they would be if the building prepaid.

Now there are three current options for providing capital grant funds for at-risk housing:

(a) *Preservation Matching Grant.* NAHT urges Congress to enact the Preservation Matching Grant to help save units and promote transfers of at-risk buildings to non-profit organizations committed to housing preservation. The proposal would provide Federal matching grants on a 2-to-1 basis to match State and local preservation funding programs.

In this Congressional session, the Preservation Matching Grant bill has been refiled as H.R. 425 by Representative Jerold Nadler and sponsored by 88 others in the House, and as S. 1365 by Senators Jeffords (I–VT), Grassley (R–IA), Chafee (R–RI), Sarbanes (D–MD), Feinstein (D–CA), Kerry (D–MA), Breaux (D–LA), Schumer (D–NY), Murray (D–WA), Dayton and Wellstone (D–MN). The Senate bill would allow direct HUD grants to nonprofits in States without a matching grant program, as recommended by NAHT. *We urge the Subcommittee to support S. 1365.*

(b) *Housing Trust Fund Grants.* Alternatively, the Roukema version of a Housing Trust Fund adopted by the House Financial Services Committee (H.R. 3995) would provide some limited grant funds to localities, which could be used for both preservation and new production of housing. Representative Sanders version of the Trust Fund proposal, which NAHT supports, adopts the same principle, but at much higher funding and matching grant levels. *If adequately funded, the Trust Fund approach could meet the need for a capital grant source for preservation as well.*

(c) *Mandate Section 531 Grants.* To date, HUD has failed to use its authority to spend recaptured Interest Reduction Payments (IRP) as capital grants to preserve at-risk housing. As a result, Congress rescinded $300 million in IRP funds last year—the same level of funding sought by NAHT through the Preservation Matching Grant. It is imperative that Congress and HUD not repeat this mistake next year. *We urge Congress to direct HUD to spend these funds, estimated to be $100 million in fiscal year 2003.*

(2) ENACT REGULATORY MEASURES TO PREVENT DISPLACEMENT AND PRESERVE AFFORDABLE HOUSING. The record shows that voluntary financial incentives are insufficient to fully halt the continued erosion of affordable housing. *Congress should reestablish a national regulatory framework to limit owners' ability to prepay and opt-out, similar to the now-defunct Title VI Preservation Program.* For example, Congress could enact rent restrictions for former HUD-subsidized buildings, require owners to accept HUD subsidy offers, and provide tenants and tenant-endorsed non-profits a Right of First Refusal when owners sell. NAHT urges Congress to consider these approaches to complement the voluntary incentives for owners provided by existing HUD programs. *It is not too early for Congressional leaders to work with NAHT to develop a long-term legislative vehicle to save our homes.*

(3) STRENGTHEN CONGRESSES' GOAL OF LAST-RESORT "ENHANCED VOUCHERS FOR ALL."

(a) *Clarify that HUD must enforce owner acceptance of Enhanced Preservation Vouchers for multiple year terms.* Congress should mandate enforcement by HUD of owner compliance.

(b) *Improve Preservation Vouchers.* Congress should make several technical adjustments to make the goal of "sticky vouchers for all" work better. For example, NAHT proposes more flexible "occupancy standards" so that Section 236 moderate income tenants are not forced out or into smaller units when tenants receive Section 8 Preservation Vouchers when owners prepay. Congress should also eliminate the problem of unnecessary "rescreening" of tenants in good standing by local Housing Authorities when voucher conversions occur. *NAHT supports language proposed by Senator Sarbanes in his Voucher bill to address these problems.*

(c) *Provide Enhanced Vouchers for tenants when mortgage terms expire.* In the near future, many buildings with 40-year HUD subsidized mortgages will near the end of their mortgage terms. Tenants in these buildings need protection from immediate displacement when this occurs. Congress should act now to anticipate this problem.

(4) MANDATE THAT HUD MAXIMIZE PRESERVATION OF AT-RISK AND HUD-OWNED HOUSING.

(a) *Mandate that HUD preserve at-risk buildings where owners must seek HUD approval to prepay or renegotiate HUD or local Use Agreements.* NAHT urges Congress to mandate HUD to use its discretionary authority to enforce use restrictions (such as flexible subsidy, Title II/VI, and local use restrictions) and procedural requirements (to review fair housing impacts, use of reserves, etc. prior to prepayment) to maximize housing preservation.

(b) *Mandate that HUD maximize preservation of buildings sold or foreclosed through HUD's Property Disposition or Foreclosure programs.* For the past 2 years, Congress has mandated that HUD preserve buildings it sells where tenants are elderly or handicapped, but not family developments, by providing grants and project-based Section 8 assistance at point of sale. Congress should extend this requirement to all buildings sold by HUD.

(5) EMPOWER RESIDENTS AND COMMUNITIES.

(a) *Drop "preemption" language in Section 232 of LIHPRHA.* Congress should amend the now-defunct Low Income Housing Preservation and Residential Homeownership Act (LIHPRHA) law to delete Section 232, which makes it more difficult to enact tenant protections at the local level in the event that Federal ones are ended through prepayment. Owners argued for this provision to protect their appraisals under the previously mandatory program. In the absence of a Federal regulatory framework such as LIHPRHA, the Federal Government should not interfere with the right of State and local governments to protect residents in accordance with local needs and conditions. (Such efforts have been adopted or are under way in Massachusetts, Washington, Oregon, California, Denver, and New York.) Similarly, Section 524(f) of the fiscal year 2000 Appropriations bill, which preempts certain local restrictions on owner dividends, may also require amendment.

(b) *Expand tenant participation.* Congress should clearly affirm that HUD, State, and owner decisions (for mark-ups and grants, for example) are significant events requiring opportunities for tenant notice and comment.

(c) *Allow HUD's technical assistance funds to be used more broadly in HUD housing.* Congress should clarify that Section 514 Technical Assistance Funds (OTAG's, ITAG's, HUD-funded VISTA Volunteers) can provide assistance to tenants in enhanced voucher buildings, prepayment-eligible buildings without Section 8, and HUD-foreclosed properties.

* * * * *

We would be happy to provide more information to the Subcommittee upon request. Thank you for holding this hearing and allowing NAHT to submit its views.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR PAUL S. SARBANES AND SENATOR JACK REED FROM JOHN C. WEICHER

Q.1. In 1997, the Congress gave HUD the authority to use Interest Reduction Payment (IRP) funds for grants for needed repairs in project-based housing, and we made this easier for HUD to do in 1999. A policy to distribute these funds was actually written and in the final stages of being issued when the Martinez Administration took over at HUD. It has been almost 2 years since the new Administration took office, and yet this policy was never implemented, and the funds never went out as intended. Unfortunately, HUD never released these funds and Congress finally rescinded $300 million in IRP funds earlier this year. Although this $300 million is no longer available for use, additional IRP funds should be available in the future. Please provide information on how much in IRP funds will be available in the next 2 fiscal years and detail your plans to implement this grant-making authority so future IRP funds can be used to rehabilitate and preserve affordable housing.

A.1. On July 12, 2002, the President submitted to the Congress a request that $100 million of IRP funds be rescinded in fiscal year 2003. The House Appropriations Committee has reported a bill that will enact this rescission, while the Senate Committee previously proposed that these funds be used to implement the rehabilitation grant program. The Department will carry out whichever policy proposal is enacted into law for 2003 and the ensuing fiscal years.

Your question makes reference to previous efforts of the Department to implement a loan program rather than the original grant program to facilitate rehabilitation efforts under Section 236(s) of the National Housing Act. The proposal was dropped when the Department was informed that budget rules would require HUD to seek additional appropriations to pay for imputed credit subsidy costs associated with these loans. For that reason, the President's budget submission has proposed that the legislative authority to offer rehabilitation loans be repealed. Again, the Department is prepared to carry out the authorities and policies that are enacted into law.

Q.2.a. We are concerned about the loss of elderly housing. Please provide data on how many Section 202 properties are at-risk.

A.2.a. The Department's current Section 202 portfolio consists of 7,051 projects. Of the 7,051 projects, the Department has determined 143 to be "troubled" or at-risk at this time.

Q.2.b. Please detail HUD's policies for providing assistance to these troubled properties.

A.2.b. HUD's current policies for providing assistance to these properties include permitting the transfer of ownership, mortgage refinancing and modifications, mortgage workouts, and the release of residual receipts.

Q.2.c. Please provide data on how many Section 202's have been foreclosed upon in the past 2 years, to whom they were sold, and what use restrictions were placed on those properties at sale.

A.2.c. See Exhibit #1.

Q.3.a. Congress requires HUD to renew Section 8 contracts at a foreclosure or disposition sale for projects that are primarily elderly or disabled unless the renewal is infeasible. Please provide data on how many of these properties have been foreclosed upon or disposed of in the past 2 years.

A.3.a. FISCAL YEAR 2001: J.C. Progress, Chattanooga, Tennessee; Number of Units: 204; Foreclosure Sale Date: 8/24/01; Sold to: City of Chattanooga. Pickwick/Royal Tower, Kansas City, Missouri; Number of Units: 233; Foreclosure Sale Date: 9/23/01; Sold to: Wilshire Realty and Investment.

FISCAL YEAR 2002: SANA Apartments, Hartford, Connecticut; Number of Units: 271; Foreclosure Sale Date: 2/1/02; Sold to: City of Hartford. Valley Housing, Appleton, Wisconsin; Number of Units: 70; Foreclosure Sale Date: 5/2/02; Sold to: Appleton Housing Authority.

Q.3.b. In how many of these cases were the Section 8 contracts renewed?

A.3.b. Since the enactment of the legislation for fiscal year 2002, HUD renewed the Section 8 contracts for both projects identified in response 3(a) above.

Q.3.c. In how many cases did HUD make the determination that renewal was infeasible?

A.3.c. Based on the dire need for affordable housing for both the elderly and the disabled throughout the Nation, HUD has made a policy determination for projects that are sold with predominately elderly or disabled residing at the project that buyers are required to maintain the project as affordable elderly and/or disabled housing for a minimum of 20 years.

Q.3.d. Please detail how these determinations were made and also include any written guidelines on how HUD makes these determinations.

A.3.d. HUD has made a decision to renew all of the project-based contracts in properties servicing the elderly and disabled clientele in accordance with the statute. As indicated above, there have been a limited number of foreclosures to date and HUD will re-evaluate this determination each fiscal year to determine if infeasibility guidelines and criteria are necessary and they will issue written guidance.

Q.4.a. We heard interesting testimony from Mr. Grow that HUD has been hostile toward preservation and has not taken necessary actions to prevent the loss of affordable housing even where community groups are interested in preserving the housing. Does HUD have written policies for dealing with a project that is at-risk of foreclosure? Please detail these policies.

A.4.a. The Department has written policies for dealing with the projects that are at-risk of foreclosure in accordance with the regulations set forth in 24 CFR Part 290. The basic operating policy for properties in risk of foreclosure, known collectively as defaulted HUD-held properties, is in Handbook 4350.1, Multifamily Asset Management and Project Servicing. HUD also issues clarifications

and may update or alter handbook policy via memorandum to meet changes in the state of the art of asset management and servicing.

In Chapter 10 of this Handbook, HUD states its intent in dealing with properties where HUD is the mortgagee as a result of a default and a FHA mortgage insurance claim. HUD-held mortgages are serviced until the note is sold or the mortgage is foreclosed.

The objectives of servicing HUD-held mortgages are: (A) Curing financial defaults and physical deficiencies after assignment by working with the mortgagor to maximize monthly remittance of payments and, if necessary, by providing mortgage relief consistent with the long-term viability of the project and the financial interests of the Government. (B) Encouraging the mortgagor to infuse funds, when necessary. (C) Ensuring that the mortgagor provides adequate management. (D) Preventing foreclosure where possible, thus, reducing the potential for further operating outlays from the insurance fund and the need for additional rent subsidies.

In Chapter 11 of the Handbook, the Department states its objectives for pursuing workouts on the defaulted HUD-held property. HUD's basic objective for projects with HUD-held mortgages is to develop a workable plan to stabilize the property, both financially and physically, and to minimize losses to the Department. The tools available to deal with a HUD-held property are identical to the Department's arsenal for at-risk Section 202's. These include refinancing, mortgage modifications, workout arrangements, transfer of ownership, release of funds from residual receipts or reserves, and when there are project-based Section 8 contracts, HUD can also consider debt restructuring through the OMHAR Mark-to-Market (M2M) Program, etc.

Q.4.b. Please provide data on how many properties and units have been foreclosed upon, how many of those properties have been transferred to nonprofits or for-profits, how many were sold with affordability restrictions, and what those restrictions are? Please include: How many times in the past 2 fiscal years has HUD decided that properties being sold through foreclosure or from the HUD-owned inventory would receive no subsidy, and that tenant-based vouchers for eligible tenants would be made available through the local housing authority?

A.4.b. For subsidized projects sold through either foreclosure or from the HUD-owned inventory, it has been the Department's policy since 1996 to provide tenant-based vouchers for eligible tenants in lieu of project-based Section 8 assistance. See attached 2001 and 2002 foreclosure charts (Exhibit #2).

Q.5.a. We are concerned by a number of instances where residents were not given proper notice of what was happening to their housing. In Texas, a property was sold at foreclosure sale with minimal affordability requirements despite the fact that notice was not adequate, and in Los Angeles, the city had to go to court to stop an owner from opting-out of Section 8 because proper notice was not given to the residents. In this instance, as we understand it, HUD approved this opt-out even though HUD requires that proper notification be given to residents. In a news article about this particular issue, advocates are quoted as blaming the problem on "a shift in Federal policy that favors giving tenants vouchers rather than re-

serving buildings for low-income residents." We are concerned that this shift in policy is leading HUD to ignore violations of its own requirements. Can you assure us that HUD is enforcing notice requirements before owners are permitted to opt-out of the Section 8 program? Please provide information an how HUD is enforcing these requirements.

A.5.a. The Section 8 Housing Assistance Payments (HAP) contracts between HUD and project owners, which provide for the project-based rental assistance, expire by their own terms. HUD does not have the legal authority to compel an unwilling owner to execute new project-based assistance contracts or to unilaterally prevent the contract from expiring. The Multifamily Assisted Housing Reform and Affordability Act (MAHRAA), 111 Stat. 1384 *et seq.,* provides tools to HUD to use in the event that an owner fails to provide adequate notice under the Federal statutes. For example, Section 514(d) of MAHRAA entitled "Tenant Rent Protections" authorizes HUD to offer to extend an expiring project-based rental assistance contract in order to give an owner sufficient time to provide the statutorily required 12-month notice to residents of their intent not to renew their project-based Section 8 contract. If an owner is unwilling to give adequate Federal notice, MAHRAA prohibits the project owners from increasing the resident's portion of the rent or evicting the residents for a period of 1-year. This, in effect, gives the residents benefit of the official notice required: It puts residents on notice that their subsidy situation may change in 1-year and it gives the residents 1-year to make alternate housing arrangements, if necessary.

In addition to the above protections, MAHRAA also provides that when a project-based rental assistance contract expires and the owner declines to renew or otherwise extend the contract, the Secretary must issue enhanced vouchers to eligible residents residing in the property at the date the project-based contract expired. The language of the statute is mandatory. The Secretary must issue the vouchers.

HUD has issued instructions to its Field Offices and Contract Administrators outlining the tenant notification requirements, and has provided specific instructions for proceeding when an owner has failed to provide proper notice. In addition to requiring that owners satisfy all statutory and programmatic notice requirements, Chapter 11, Section 11–4, of the Guide requires that owners who wish to opt-out provide HUD with a completed "Contract Renewal Request Form" not less than 120 days prior to contract expiration, confirming the decision to opt-out and certifying that the statutory notification requirements have been met (see Guide, Chapter 11, Section 11–4(F), and Attachment 3A–2 (Contract Renewal Request Form)). Upon receipt of this form, and if proper tenant notice was provided, HUD begins the process of making enhanced voucher assistance available to all eligible tenants residing in an assisted unit on the date of contract expiration or termination.

Additionally, individual tenants and tenant organizations are involved in the notification process from the outset. HUD has also published the Tenant Rights and Responsibilities Brochure, which provides a tenant with information regarding the tenant notification process.

In instances where faulty notice has been issued, HUD provides the owner with the option of a short-term contract, which will have a term sufficient to meet a full 1-year notice period. Owners who decline to enter into the short-term contract must permit the tenants to remain in their units without an increase in the amount of rent that the tenant must pay.

Enforcement Examples: Between fiscal year 2000 and 2002, there were approximately 74 projects, comprising 3,399 units, where HUD offered and the owner accepted an extension of the terminating contract in order to meet the required tenant notification.

Q.5.b. Where improper notice has been given to the residents HUD does not have to pay the owner the higher rents under enhanced vouchers. Has HUD used this tool to force compliance with notice requirements? Please provide information on when HUD has taken these actions and in how many cases.

A.5.b. The statute requires that HUD issue enhanced vouchers to eligible tenants residing in the property at the date the project-based Section 8 contract expires. To date, this tool has not been used by the Department to force compliance with the tenant notice requirements. However, significant revisions to the Section 8 Guide are currently under development and the revised guidance will address this matter. The revisions include guidance on how to address an owner who fails to issue proper 1-year notification to HUD/CA and the tenants. Legally, the owner must permit the tenants to remain in their units without increasing their portion of the rent for whatever period of time is necessary to meet all of the notification requirements.

In cases where improper notice has been provided, eligible families residing in the property will still be issued enhanced vouchers when the contract expires. The family may use the voucher to remain in their current unit or they may elect to use the voucher to move to another property. Should the family elect to remain in their current unit, the voucher housing assistance payments contract may not commence until the full 1-year notice has been met. The effect of this action is that the owner will not receive any voucher assistance payments until proper notice has been provided to the tenants.

Q.5.c. Your statement indicates that this issue will be clarified when HUD issues revisions to the Section 8 Renewal Guide "within the next few months." When does HUD plan to issue the revision? Please provide us with a copy of these revisions.

A.5.c. HUD is in the process of finalizing significant revisions to the Section 8 Guide and submitting the revisions through the Department's internal clearance process. Upon completion of the clearance process, the revisions will be made available and HUD anticipates issuing the revised Section 8 Guidebook during the second quarter of fiscal year 2003. In the area of tenant notification, the revisions will include guidance that will require HUD's offices to review all tenant notification letters within 30 days of receipt. If the owner does not comply with the statutory requirements, the owner will be advised that a new notification letter must be issued. If a faulty notice was provided, the statute requires that the owner must permit the tenants to remain in their units without an in-

crease in the portion of rent the tenant pays until a full 1-year notice period has elapsed.

Q.6.a. Under Section 250 of the National Housing Act, HUD may only allow prepayment in those situations where HUD finds that "the project is no longer meeting a need for rental housing for low-income families." How many prepayments has HUD allowed under Section 250?

A.6.a. Section 250(a) applies only to projects that receive some form of subsidy under or in connection with a mortgage (i.e., Sections 236 and 221(d)(3) BMIR projects and also projects receiving Rent Supplement payments). Accordingly, where only the Section 8 assistance or no assistance is provided, Section 250(a) is not applicable. The 128th *Congressional Record* S. 4078 supports this interpretation.

HUD has not approved any prepayments based on determination under Section 250(a); rather, HUD has made a determination that all projects that fall under this requirement are serving a low-income housing need. Based on that determination and recognizing the need for capital infusion into this type of housing in order to preserve the affordable resource, HUD has allowed prepayments only in those cases where the owner has agreed to ensure the property remains available to low-income families in the area. This has been accomplished by placing a Deed Use Restriction on these properties that restricts the use of the property to the same conditions required under the mortgage insurance program.

Q.6.b. Where prepayments have been allowed, how has HUD made the determination that the housing was no longer needed? Please provide the written guidelines that HUD uses to make these determinations.

A.6.b. As stated above, HUD has decided that any property subject to Section 250(a) is to be kept affordable and has used use restrictions to maintain affordability.

Q.6.c. Please provide information and data on each prepayment allowed under Section 250 in the last 2 years.

A.6.c. As stated above, HUD has not approved any prepayments under Section 250.

Q.7. Last year, we passed the "Mark-to-Market Extension Act," which the President signed into law in January of this year. Section 613 of the law requires HUD to ensure that rent levels offered to owners through the project-based program are the same as the rent levels offered through enhanced vouchers. We included this provision because we heard numerous reports, from both owners and residents, that owners were getting higher rents through the enhanced voucher program, thereby giving them an incentive to opt-out of their long-term affordability commitments. What steps has HUD taken to implement Section 613 of the law, and what have the results been? Please provide data and specific examples.

A.7. Section 613 required HUD to ensure rent levels are "reasonably consistent and reflect rents for comparable unassisted units." The three types of Section 8 assistance affected are project-based Mark-to-Market renewals with market rents set by the OMHAR, project-based renewals with rents determined by the Multifamily

Housing, and enhanced vouchers with rents set by owners and approved by public housing agencies (PHA) according to a "rent reasonableness" determination. While rent determinations are property specific and can only be determined within a range of certainty, a reasonable level of consistency in these determinations is critical in order to ensure the integrity of Federally-assisted housing programs.

Early on in the Mark-to-Market Program, there was, in fact, a systemic problem with inconsistency between OMHAR's and Multifamily Housing's rent determinations on project-based renewals. This has been addressed by improved coordination between the offices. OMHAR has adopted Multifamily Housing's appraisal standards (published in Chapter 9 of the Section 8 Renewal Guide), and Multifamily Housing's management has given priority to ensuring appropriate referrals to OMHAR. As a result, there has been a marked increase in the percentage of properties with Section 8 expirations that are referred to OMHAR. During the first 3 quarters of fiscal year 1999, 15 percent of these properties were referred to OMHAR. During the first 3 quarters of fiscal year 2002, 41 percent of projects with expiring contracts were referred. For comparison, portfolio stratification modeling (provided to Congressional staff and the GAO in August 2001) suggested that between 40 and 45 percent of the portfolio has above market rents. Additionally, a number of properties are coming back into the M2M pipeline under the "look back" authority in Section 612(f).

Rents approved by the PHA's for enhanced voucher units do not appear to be a systemic or continuing problem. By statute, PHA's must ensure that the owner's requested rent is reasonable in comparison with similar unassisted units in the market area. Congress did amend Section 8(t) in HUD's fiscal year 2001 Appropriations Act to allow the Department to impose additional reasonable restrictions on rents for enhanced vouchers in order to address concerns that enhanced vouchers might encourage owners to leave Multifamily Housing's affordable housing programs. However, subsequent legislation rendered this authority meaningless (Section 902 of Public Law 106–569), by providing that any limitation could not be considered "reasonable" if it could have an adverse impact on families.

As you note, there were concerns last year that some PHA's were approving enhanced voucher rents that were materially greater than the Department's determination of market rent, and thus affordable housing units were lost when the owners opted-out of their Section 8 contracts. OMHAR has emphasized to the PAE's the requirement to share market rent determinations with the PHA's, and HUD's Office of Public and Indian Housing (PIH) has advised PHA's and PIH Field Office staff on a case-by-case basis to not approve rents exceeding those rents unless there is a clear material and documented flaw. More formal guidance will be issued to that effect in a forthcoming PIH Notice. A list of M2M properties that opted-out of their Section 8 contracts is attached (Exhibit #3).*

Q.8. Another provision of the M2M Extension Act allows the second mortgages created by the restructuring to be assigned to the

*Held in Committee files.

nonprofit or Government agency that is acquiring the project. The debt assignment would be in lieu of forgiving the debt altogether, so there is no cost to the Federal Government. In certain circumstance, the assignment is preferable because it helps the nonprofit receive tax credits for rehabilitation. Please detail how this provision has been put into effect by HUD.

A.8. The new authority to assign the debt resulting from the M2M restructuring was internally reviewed and approved for implementation in June 2002. The M2M Operating Procedures Guide (Appendix C—Qualified Nonprofit Purchasers) was amended in early July to include the administrative procedures needed to implement the debt assignment authority. The new authority has been well received by the nonprofit community. To date, the Department has closed a portfolio of 5 loans involving debt assignment, with a second portfolio of 16 loans near closing. Six more projects have been identified for a potential purchase and debt assignment. It is too early to estimate the number of debt assignment transactions that will close over the next 2 years. When HUD closes a restructuring with the existing owner, it allows a 3-year period for a qualified nonprofit to purchase the property and apply for debt forgiveness or assignment.

Q.9. Does HUD consider an owner's refusal to agree to reasonable rents established by a PHA, failure to repair units to meet Housing Quality Standards, or charging of new market-rate security deposits violations of a tenant's Federal statutory right to remain? Please explain.

A.9. As required by statute, an assisted family may elect to remain in the same project after expiration of the project-based HAP contract. Voucher assistance may only be paid if the rent is reasonable and the unit meets the voucher housing quality standards. These voucher requirements do not apply unless the owner has entered into a voucher HAP contract. There is no Federal restriction on the amount of the owner security deposit for a nonvoucher family that elects to remain in the project. (The PHA has discretion whether to limit the security deposit for a voucher participant.)

There may be cases where the owner disputes the "reasonableness" of the enhanced voucher rents, as established by the PHA. If, after discussion and negotiation with the PHA, the owner and the PHA are unable to reach an agreement on the appropriateness of the enhanced voucher rent, no contract will be executed. Upon expiration of a project-based Section 8 contract, the Department does not have the authority to require an owner to execute a contract at rents less than what the owner is requesting. In these cases, tenants will be provided regular vouchers and will be required to seek other housing.

Q.10. In light of the required certification in the opt-out notice that the owner will accept enhanced vouchers, if an owner later refuses to honor the tenant's statutory right to remain by executing voucher assistance contracts for all of the affected units, what enforcement actions could the Department take, both prior to and after the conversion? Does the Department need additional authority to protect tenants?

A.10. The family may raise claimed violation of the statutory election to remain either as a defense in the owner's action for eviction or as a basis for injunctive relief against the owner. HUD does not need or seek additional statutory enforcement authority.

Q.11. As recognized by HUD's Guide, the tenant's right to remain continues until the tenant commits a breach of the lease, notwithstanding the expiration of any lease term. This is different than the current rule governing ordinary Housing Choice Vouchers, where no cause is required at the end of the lease term. What steps has the Department taken to ensure that tenants, PHA's, and owners are informed of this difference so that tenants are not displaced later without cause?

A.11. Currently, the owner's lease in the Housing Choice Voucher Program may provide the owner with the authority to terminate the tenancy upon expiration of the lease term. However, the tenant's right to remain with enhanced voucher assistance as a result of an opt-out is the same as if the project-based Section 8 assistance was still in place.

The Department, in both the Section 8 Renewal Guide and PIH Notice 2001–41 *(Section 8 Tenant-Based Assistance [Enhanced and Regular Housing Choice Vouchers] For Housing Conversion Actions —Policy and Processing Guidance),* is consistent with instructions regarding the enhanced voucher family's right to remain. Guidance in both the Renewal Guide and Notice 2001–41 provides that ". . . the owner may not terminate the tenancy of a family that exercises its right to remain except for a serious or repeated lease violation or other good cause."

In addition, in meetings and training sessions with the various program participants (PHA's, residents, and owners), the Department emphasizes the differences between the enhanced voucher and the regular voucher rules and provides technical assistance when necessary.

Q.12.a. Concerning the eleven properties owned by the HEDCO located in Woonsocket and Central Falls, Rhode Island: By way of clarification, the 11 properties are each owned by a separate, single purpose entity (either corporation or as a general or limited partner in a limited partnership). What actions did HUD take to ensure the owner provided proper opt-out notices under both Federal and State law prior to the expiration of the Section 8 contracts?

A.12.a. If an owner does not plan to participate in the Section 8 project-based program and renew the contract at expiration, the owner must provide to the Department at least 1-year notice before the contract expiration date of their intent not to participate in the Section 8 project-based program. Section 8(c)(8) of the U.S. Housing Act requires that:

> Not less than 1-year before terminating any contract under which assistance payments are received under this Section, other than a contract for tenant-based assistance under this Section, an owner shall provide written notice to the Secretary and the tenants involved of the proposed termination. The notice shall also include a statement that, if the Congress makes funds available, the owner and the Secretary may agree to a renewal of the contract, thus

> avoiding termination, and that in the event of termination the Department of Housing and Urban Development will provide tenant-based rental assistance to all eligible residents, enabling them to choose the place they wish to rent, which is likely to include the dwelling unit in which they currently reside.
>
> 42 U.S.C. § 1437f(c)(8).

The Federal litigation *(People to End Homelessness, et. al.* v. *Martinez, et. al.,* U.S.D.Ct.,D.R.I., No. 01–0269T) involved four "scattered-site" housing projects (known collectively as "the Develcos") in Woonsocket, Rhode Island, all with HUD-insured mortgages and rental assistance to the tenants originally under the Section 8 Loan Management Set Aside Program and then under the Section 8 Voucher Program.

The project-based Section 8 contracts for the Develcos expired by their own terms on May 31, 2001. HUD's Section 8 Guidebook provides that "Section 8 project owners must also comply with any State or local notification requirements." This provision is meant only to remind owners to comply with any applicable State or local requirements. The Section 8 Guidebook also states, "Owners should check with their appropriate local authorities to find out about such requirements." This provision does not place an affirmative legal obligation on HUD to ensure that all owners with Section 8 HAP contracts comply with State law when opting-out (See *Kenneth Arms Tenant Association, et. al.* v. *Martinez*). Rather, these provisions are a reminder to property owners.

HUD has no statutory or regulatory obligation to "enforce" Federal or State requirements for notice of HAP contract termination against owners in particular cases. In the case of the four Develco properties, HUD believes that the owner's notice provided to the residents was adequate under the applicable Federal law. HUD was not a party to the litigation brought in the State Court of Rhode Island in which the residents had challenged the owners' decision to opt-out of their Section 8 project-based contracts. Additionally, neither the Federal nor State courts had imposed any restriction upon the Department that would have impacted the contract opt-outs.

In regard to the other seven projects, the project-based Section 8 contracts expired by their own terms on August 31, 2001 (Mercedes Apartments IV and Sans Souci Apartments I), on September 30, 2001 (David Apartments, Mercedes Apartments II, Polonaise Apartments and Roger and Roger Apartments), and on January 31, 2002, for the Vulcan Apartments. HUD also made the determination for these projects that the notice provided to the residents was adequate under the applicable Federal law.

Q.12.b. Why did HUD provide enhanced vouchers to the owner when the owner had clearly failed to comply with both the Federal and the State notice requirements, contrary to your written statement? Please explain how this expressed position is consistent with the Department's position in the Federal litigation regarding this matter.

A.12.b. The Department does not agree with the assertion that the owner failed to comply with the Federal notice requirements. On

the contrary, HUD determined, through careful evaluation, that the Federal notice given to the residents and to the Secretary was adequate.

However, even if the notices given by the owners were not adequate, HUD would still have been compelled by Section 524(d)(1) of the MAHRAA to issue enhanced vouchers to all eligible residents residing at the projects on the date in which the project-based Section 8 contract expired.

This is precisely the position put forth by the Department in the course of the Federal litigation, *People to End Homelessness* v. *Martinez*. The Court indicated in its Memorandum and Order dated March 29, 2002, that "the principal issue presented was whether the owners' alleged failure to give sufficient advance notice of their intention to 'terminate' their contract with HUD requires HUD to continue providing project-based assistance for the complex(es)." The Court answered the question in the negative finding that the plaintiffs (tenants) were unable to identify any statutory provision requiring HUD to continue project-based assistance to a housing complex if the owner fails to provide proper notice that it is "terminating" its contract to participate in the program. The Court stated that HUD was required by MAHRAA to issue enhanced vouchers to the tenants at the expiration of the project-based Section 8 contract irrespective of whether the owner provided adequate notice to the tenants (though in this case HUD determined that the notice was adequate).

Q.12.c. Prior to selling the HUD-held mortgages on at least five of the properties (two that are involved in the Federal litigation and three in the State case), did the Department evaluate: (1) whether such sale was in compliance with existing Federal laws and regulations; (2) what protections under the Regulatory Agreement might be lost; (3) the impact of the mortgage sale on the tenants' claims under Rhode Island law and possible preservation of the property; and, (4) the fair housing implications of this action?

A.12.c. (1) The mortgages sold in the Multifamily and Healthcare Loan Sale 2002–1 were sold in compliance with all existing Federal laws and regulations. The authority of the Secretary to sell the mortgages sold in the Multifamily and Healthcare Loan Sale 2002–1 is set forth in Section 207(k) of the National Housing Act (12 U.S.C. § 1713(k)), Section 203(k) of Housing and Community Development Amendments of 1978, as amended (12 U.S.C. § 1701z–11), and Section 204 of the fiscal year 1997 Appropriations Act, as amended (12 U.S.C. § 1715z–11a).

The mortgages sold in the sale were all unsubsidized. Authority for the sale of HUD-held multifamily mortgages is found in Section 204 of the fiscal year 1997 Appropriations Act, as amended, which authorizes the Secretary to sell "multifamily mortgages held by the Secretary on such terms and conditions as the Secretary may determine, notwithstanding any other provision of law."

(2) The Regulatory Agreements between the owners and HUD terminated when the mortgage loans were sold. The Department was aware that those provisions of the Regulatory Agreements that benefited the tenants, such as the requirement that the owner maintain reserve for replacement accounts, would no longer remain

in effect. However, under existing regulations governing the sale of HUD-held mortgages securing unsubsidized projects, HUD had no obligation to continue to impose the tenant protection provisions of the Regulatory Agreements after the loans were sold.

(3) The Department was not required to assess any impact of the mortgage sale on the tenants' claims under Rhode Island State law and on the possible preservation of the property. As the Department understands, the project-based Section 8 contracts for the Develco properties expired by their own terms on May 31, 2001. As stated earlier, HUD has no responsibility to determine whether the notice provided to the tenants met the Rhode Island State notice requirements.

(4) The Department complied with the fair housing requirements set forth in 24 CFR 290.39 in connection with the sale of loans in the Multifamily and Healthcare Loan Sale 2002–1. HUD included in the Loan Sale Agreement for each purchaser a provision to implement the regulatory requirement regarding nondiscrimination in admitting certificate and voucher holders. That provision requires the purchaser of any delinquent mortgage loan, and its successors and assigns, to record a covenant running with the land as part of any loan restructuring or final compromise of the mortgage debt and to include a covenant in any foreclosure deed in connection with the mortgage. The covenant must provide that the project owner shall not unreasonably refuse to lease a dwelling unit offered for rent, offer to sell cooperative stock, or otherwise discriminate in the terms of tenancy or cooperative purchase and sale because any existing or prospective tenant or purchaser is a certificate or voucher holder.

Q.12.d. How does the Department justify the significantly higher "market" rents provided to the owner by the PHA under the enhanced voucher program on some of the HEDCO properties, when compared with the "market" rents for renewal of the project-based contract offered by HUD or OMHAR? Shouldn't these amounts be roughly comparable? What steps is the Department now taking to avoid similar discrepancies in the future?

A.12.d. The Department is aware that under current law, the method of calculating reasonable rents for project-based Section 8 HAP contracts (under the MAHRAA) and for tenant-based enhanced vouchers (under Section 8(t) of the U.S. Housing Act of 1937) may differ. In the case of a restructured project with project-based Section 8 participating in the Mark-to-Market Program, HUD establishes the rent level at rates it determines to be "comparable" to the rents currently being charged by owners of comparable unsubsidized properties. See § 514(g) of MAHRAA.

However, if an owner of a project with an expiring Federal rental assistance contract does not agree to extend the contract, § 514(d) of MAHRAA provides that the Secretary shall make tenant-based assistance available to tenants residing in units assisted under the expiring contract at the time of expiration. The tenant-based assistance is in the form of enhanced vouchers. When Section 8 rental subsidy is tenant-based, the local housing authority administers the subsidy and determines tenant qualification (as opposed to project-based Section 8 rental subsidy in which the project owner

receives the subsidy and determines tenant qualifications.) The housing authority is also responsible for making the determination that the rents charged for the units that eligible voucher holders desire to reside in are "reasonable rents (which rent shall include any amount allowed for utilities and shall not exceed comparable market rents for the relevant housing market area)." Section 515(c)(3) of MAHRAA.

While it is logical to conclude that the rent levels for project-based and tenant-based Section 8 may differ for the same project based upon the fact that comparable rents are calculated by the different entities, it is not the Department's intention for tenant-based subsidies to far exceed project-based subsidies. This is a situation where the Administration is carefully analyzing and working to ensure that on future project-based Section 8 opt-outs, the comparable rents for enhanced voucher units are comparable to maximum project-based rent levels for restructured projects and expect to correct the problem as quickly as possible.

Q.12.e. For how many of these properties did the owner prepay? Please describe the process. Were you aware of the State lawsuit regarding these properties?

A.12.e. The Department's records indicate that the owner has only prepaid the Section 221(d)(3) Market Rate Mortgage on the Roger and Roger Apartments at this time. Pursuant to the Section 221 (d)(3) Market Rate Mortgage Program, the owner must notify the Department 30 days prior to the prepayment of the mortgage. The Department is not required to approve the prepayment of the mortgage and has no statutory authority to stop the prepayment if proper notice was given to HUD.

The Department was aware that there was ongoing State court litigation involving David Apartments, Mercedes II Apartments, Mercedes IV Apartments, Sans Souci Apartments, Polonaise Apartments, and the Vulcan Apartments. However, the Court had not imposed any restrictions upon the Department, which would have impacted the prepayment of the mortgages or selling the mortgage notes.

2002 Foreclosures
(Does not include assisted living, nursing homes, 202's or bankruptcy liquidations)

Property Name	Units	Non-profit	For profit	Local Gov.	Affordability Restrictions
Albany Landing	120		x		note 1
Atlantic Properties	91		x		x
Bedford Street	91		x		note 2
Bennett Street	6		x		note 2
Brotherhood	50		x		note 2
Church Hill Village	40		x		x
Clinton Hill	50		x		x
Dove Meadows	474			x	x[3]
Fairlane Meadows	52			x	x
Grove Apts.	42		x		x
Hill View Heights	100		x		note 1
J.C. Progress	204			x	x
Landerville	16		x		x
Lockwood Plaza	209			x	x
Metro Manor	148		x		x[4]
N.31 Va. Ave.	38		x		x
National Properties	52		x		note 2
New Carver I	100		x		x
New Carver II	108		x		x
Northfield Manor	48		x		note 1
Ridgeview Manor	88			x	x
Reiman Block	27		x		x
Sentinel	120		x		note 1
Silver Creek	37		x		note 2
Stephens Square	93	x			x
Wade Manor	40		x		x
West St. Apts.	65			x	x
Willard J. Price	191	x			x
Shelby Manor	44		x		x
	2744				

note 1: Non-subsidized
note 2: The costs to rehab are such that monthly debt service needed to amortize the costs of rehab, operating expenses and provide a reasonable return to the owner cannot be provided by the after sale rents.

[3] 250 of 474 units sold with use restrictions
[4] 30 of 48 units sold with use restrictions

Exhibit #1

Property Name	Location	# Units	Fiscal Year	Comments
Bethesda Manor II	Plainview, TX	12	FY01	Sold to Wayland Baptist University Maintained as affordable housing for 20 years.
Kennilworth Park Plaza	Portland, OR	77	FY01	Sold to city of Portland Maintained as affordable elderly housing for 20 years.
Project Independence	Arkansas City, KS	49	FY01	Sold to Arkansas City Maintained as affordable housing for 20 years.
NMARC	Santa Fe, NM	6	FY01	Sold to the Santa Fe Civic Housing Authority No use restrictions.
Monastery	Way Sitka, AK	24	FY01	Sold to Baran of Island Housing Authority Maintained as affordable elderly housing for 20 years.
Morningside Village	Alcester, SD	31	FY01	Sold to city of Alcester Maintained as affordable housing for 20 years.
Elmwood Group Home (Tenco Group Homes, Inc.)	Ottumwa, IA	15	FY01	Sold to Area XV Multi-County Housing No use restrictions.
Edgewood/Eldercrest	Youngstown, OH	147	FY01	Sold to city of Youngstown. Maintained as affordable elderly housing for 20 years.
Tiffin VOA	Tiffin, OH	20	FY01	Sold to Seneca County No use restrictions.
Rochdale Court Apartments	Detroit, MI	70	FY02	Sold to the city of Detroit Maintained as affordable housing for 20 years.
Four Freedoms	Detroit, MI	320	FY02	Sold to Madrix Realty Group. Maintained as affordable elderly housing for 20 years.

Exhibit #2

2001 Foreclosures
(Does not include assisted living, nursing homes, 202's or bankruptcy liquidations)

Property Name	Units	Non-profit	For profit	Local Gov.	Affordability Restrictions
Lambda RHO	80		X		x
Oak Tree Villa	120		X		
RAC Gardens	62	x			x
Fairmont	9		x		x
SANA Apts.	271			x	x
Campus Manor	68			x	x
Freedom Apts	308			x	x[1]
Parkside	48		x		x
Evening Star	35		x		x
School House 181	100		x		note 2
Cypress Point	120		x		note 1
Kentucky Towers	275		x		note 1
Cora	22		x		note 1
Brick Towers	324		x		note 3
Holiday Lakes	208			x	x[2]
Melrose	42			x	x
Keystone Farms	90		x		note 1
Carr Street	11			x	x
Riverbend Apts.	40		x		note 1
Pinery Townhouses	202		x		note 1
	2435				

note 1: Non-subsidized
note 2: The costs to rehab are such that monthly debt service needed to amortize the costs of rehab, operating expenses and provide a reasonable return to the owner cannot be provided by the after sale rents.
note 3: The costs to rehab are such that monthly debt service needed to amortize the costs of rehab, operating expenses and provide a reasonable return to the owner cannot be provided by the after sale rents, and property was determined not feasible due to environmental factors that cannot be mitigated by HUD or the Purchaser.

[1] 207 of 308 units sold with use restrictions
[2] 125 of 208 units sold with use restrictions

Dedicated solely to ending America's affordable housing crisis

October 15, 2002

The Honorable Jack Reed
United States Senate
Washington, DC 20510

Dear Senator Reed:

The National Low Income Housing Coalition (NLIHC) would like to thank you for holding hearings in the Housing and Transportation Subcommittee of the Committee on Banking, Housing and Urban Affairs on October 9, 2002 on affordable housing preservation. NLIHC believes that preservation of our existing affordable housing should be a central element in our nation's housing policy. Given the gap that already exists in housing available and affordable for the poorest families, as documented by the Millennial Housing Commission, it is essential that Congress and HUD take action to preserve our existing assisted housing stock.

We appreciate your leadership in creating an opportunity for discussion on the record of the issue of preservation generally and HUD's role in particular. We have a few comments to add to and amplify the testimony presented at the hearing.

HUD's Reinterpretation of Section 8 Housing Assistance Contracts with State Housing Finance Agency Financing

We strongly support the testimony of Katherine Hadley, representing the National Council of State Housing Agencies, on the issue of HUD's recent reinterpretation of Section 8 contracts entered into between 1975 and 1980 on properties financed by state housing finance agencies. We fear, as we know you do, the effect that HUD's current position could have on over 100,000 units of assisted housing around the country.

We ask that Congress advise HUD to delay in issuing guidance, given the significant consternation on Capitol Hill and among state governments and advocacy organizations around the country over this reinterpretation. We hope that your input, both in writing and at the hearing, will cause HUD to reverse its reinterpretation and we ask that you continue to urge HUD to do so. Should HUD continue to follow its reinterpretation of the contracts, we ask that Congress overturn such an interpretation legislatively.

Mortgage Sales

A further important preservation issue raised by the testimony of Jim Grow of the National Housing Law Project involves the recent sale by HUD of subsidized and insured mortgages for affordable rental projects. We believe HUD's disposition of these mortgages, without continuing

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affordability restrictions, violates federal law and is further evidence of HUD's ongoing efforts to eliminate, rather than preserve, the supply of existing affordable units, particularly in tight rental housing markets. We urge you to take immediate action to ensure that HUD remedies these illegal mortgage sales and prevent the future occurrence of any similar mortgage sales that result in the loss of affordable rental units.

Interest Reduction Payment Rehabilitation Funding

All of the witnesses made reference to the use of recaptured interest reduction payments (IRP) on prepaid Section 236 properties for the rehabilitation of other eligible assisted properties. We were extremely disappointed that the Fiscal Year 2002 Supplemental Appropriations Act rescinded $300 million of IRP funds, especially given HUD's inaction over the past five years in implementing the use of these funds as Congress intended. The Fiscal Year 2003 Appropriations Bill passed by the Senate Appropriations Committee would make $100 million of recaptured IRP funds available for rehabilitation; the Appropriations Bill passed by the House would again rescind the recaptured IRP funds.

We hope that you work in support of the Senate's version of the Appropriations Bill as it moves through Congress. Given past experience, we also anticipate that HUD will require prodding to release the IRP funds, should they become available once again for rehabilitation.

ITAG and VISTA Programs

Our experience has shown that, at the local level, preservation succeeds through the efforts of committed non-profit organizations working in partnership with tenants. To support these preservation activities, the VISTA program provides for outreach to tenants in eligible properties and the Intermediary Technical Assistance Grant (ITAG) program funds predevelopment planning and resident capacity building, in preparation for preservation purchases.

Both the VISTA and ITAG programs have been frozen for more than a year in the wake of concerns over a possible Anti-Deficiency Act violation over a year ago, even though it was subsequently determined that no such violation had occurred. Congress should urge HUD to resume these programs immediately and to ensure that it will be prepared to administer VISTA, ITAG and Outreach and Technical Assistance Grants for Fiscal Year 2003.

On behalf of NLIHC's Preservation Committee, thank you for your consideration of the issues discussed in this letter and for your commitment to the preservation of our nation's affordable housing stock.

Sincerely,

Sheila Crowley, Ph.D.
President

STATEMENT OF MICHAEL BODAKEN

ON BEHALF OF

STEWARDS OF AFFORDABLE HOUSING FOR THE FUTURE

OCTOBER 16, 2002

Introduction

The following testimony on the critical need for preservation of multifamily homes is presented on behalf of Stewards of Affordable Housing for the Future ("SAHF," pronounced like "safe").

Formed in June of this year, the founding members of SAHF are: The National Affordable Housing Trust, Mercy Housing, Inc., National Church Residences, Inc., the NHP Foundation, NHT/Enterprise Preservation Corporation, Preservation of Affordable Housing, Inc., Retirement Housing Foundation and Volunteers of America.

The founding members are all nationally active owners of affordable housing, committed to the mission of providing and preserving affordable homes for the long-term, keeping them well maintained and enhancing resident services for the people who live there. Together, the members of SAHF own and control over 62,000 affordable apartments in 41 States the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. *(See Exhibit A.)**

Of the apartments owned by the SAHF, 34,460—more than half—are Federally-assisted and/or insured. The vast majority of those involve some sort of HUD insurance or subsidy. Because this is the Subcommittee of jurisdiction for the policies of HUD, we are especially grateful that its Members are obviously concerned about the preservation and improvement of HUD assisted and/or insured multifamily stock. As we explain below, this housing is a unique resource. Once lost, it is virtually impossible to replace.

Once it is shown that this stock is worth saving—and it *is* worth saving—the next question is, "What are the critical components to its preservation?" We believe the answer should be guided by the following principles:

- HUD should *strongly* encourage the preservation of this stock where it is of value to the residents and the community in which it operates.
- HUD should encourage the new stewardship of these assets in interested owners, especially national and regional nonprofit owners with the capacity to own and recapitalize HUD multifamily real estate. SAHF is especially concerned that HUD does not recognize the benefits of long-term ownership by strong, mission driven, nonprofit organizations. Too often, Federal funds have been used to purchase affordability multiple times on the same property. In particular, we believe that HUD has not taken into account independent resources that organizations like members of SAHF can bring to rehabilitation and strengthening of HUD-assisted developments.
- Congress should immediately make clear to HUD that its new "interpretation" of the automatic termination of HUD subsidies upon refinance of the State housing financed, Section 8 developments, constructed between 1975–1979, is contrary to Congressional intent and practice over the past 20 years.
- Congress should take steps to assure the financial markets that Section 8 properties will continue to receive ongoing subsidies, so long as those subsidies are at or below market.

This testimony will cover three areas:

1. First, why preserving Federally-assisted housing is important.

2. Second, how members of SAHF are able to help HUD meet its responsibility to preserve this stock by securing additional State and local funds to maintain and improve Federally-assisted housing.

3. Third, a summary of the SAHF's specific recommendations on preservation of HUD-assisted and/or insured, multifamily housing, focusing in particular on:

   a. The need for HUD to assure nonprofit organizations that it will permit distributions to nonprofits on the same basis as to for-profit owners.

   b. The need for HUD to provide predictable access to "up to 20" year Section 8 contracts, subject to annual appropriations.

Preserving the Stock of Federally-Assisted Housing is Crucial

The demand for decent, safe, affordable housing remains high, while the supply of such housing is shrinking: According to a recent State of the Nation's Housing Report, "The red-hot economy has done little to relieve the housing problems of low-

*All Exhibits held in Committee.

income households."[1] Federally-subsidized units continue to disappear: Between 1995 and 2001, the number of directly Federally-subsidized units fell by over 200,000 units. Contracts on another one million units will expire within 5 years. According to a December 2001 report by the Center for Housing Policy, "Housing America's Working Families," there are 13.7 million families currently experiencing critical housing needs, meaning that they pay more than half of their income for housing and/or live in a severely inadequate unit.

Action must be taken *now* to preserve and to improve affordable rental homes because:

- Any additional loss of affordable homes will have an adverse impact on the growing number of economically disadvantaged households in this country. According to this year's HUD report "Waiting in Vain: An Update on America's Rental Housing Crisis," time on waiting lists is growing, the number of families on the lists is increasing, and the lowest-income families and seniors have limited options.
- The affordable housing stock that is most susceptible to opting-out of long-term affordability requirements is the housing stock that is most irreplaceable. Conversion opportunities are greatest for housing located in strong market areas. In these areas, the barriers to entry of zoning restrictions and high land costs are also greatest. The secret story that the numbers do not tell is that the affordable housing stock that is lost is lost in communities in which replacement affordable housing is not likely to ever be built. In order to compete for scarce resources, new production is inexorably driven to areas in which the zoning and cost barriers to entry are lowest.
- *Section 8 contracts are expiring en masse,* adding to the complexity of the preservation dilemma. Two-thirds of all project-based Section 8 contracts will expire in the next 4 years, totaling approximately 6,000 properties containing *one million subsidized apartments.* The expiring contracts are geographically diffuse: In 44 States, more than half of Section 8 units will expire in the next 5 years. Many owners are prepaying their mortgages or opting-out of the Section 8 program. Those that do renew their contracts must do so every year, dependent upon funding allocated by the Congress. The consequences of this unstable atmosphere of shifting policy are falling upon the shoulders of our Nation's poor. *(For a map color coded by State describing Section 8 expirations, please see Exhibit B.)*
- More than 2,000 project-based Section 8 units are lost each month to opt-outs, and conversion to unsubsidized housing. According to the National Housing Trust, nearly 200,000 such apartments have been converted to market rate already. *(See attached map, Exhibit C.)*
- According to HUD, the average income of those residing in HUD subsidized housing is less than $10,000/annually. Obviously, these families and elderly households do not have an effective housing choice in the unregulated housing market.
- According to HUD, *minority households occupy more than half of these apartments.* Hence, these families will disproportionately shoulder the adverse affects of additional losses of Federally-assisted and insured homes.
- Rent increases are outpacing inflation in *all* 23 metro areas surveyed by the CPI as of 2000.
- In the 1970's, this Nation produced 200,000 units per year affordable to low-income households. Even with the recent tax credit boost, we currently produce *less than half* that amount.
- As noted by the Millennial Housing Commission, the cost of preservation is less expensive than new construction. New tax credit housing amounts to approximately 80,000 units. *The cost of replacing the 120,000 "lost" units is much greater than maintaining that stock.*
- Maintaining and renovating existing housing not only helps existing renters, but also helps maintain healthy communities.[2]

Thus, the preservation of existing affordable housing is a critical goal. There are a variety of ways to accomplish this important public policy objective. The advantage of a multifaceted preservation approach is that the investment can create a stock of *permanently* affordable housing.

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[1] "State of the Nation's Housing 2000," Joint Center for Housing Studies of Harvard University, p. 23.

[2] Meeting Our Nation's Housing Challenges, Report of the Bipartisan Millennial Housing Commission Appointed by the Congress of the United States, 2002, pp. 31–33.

If HUD Stands Ready to Preserve Properties, Members of SAHF are Able to Assist HUD in Recapitalizing HUD Stock

From around 1966–1984, HUD housing programs allowed the private sector to produce nearly two million affordable housing units located in nearly every nook and cranny of the Nation. Today, much of that stock is in need of repair and new stewardship.

It is our collective and respectful observation that the Subcommittee should make clear to HUD that its mission is not to stand idle while HUD rental housing either converts to market rate conventional housing or becomes more and more deteriorated. Instead, as the Congress has made clear for over 15 years, with statutorily provided programs ranging from LIHPRHA to Mark-to-Market to Interest Reduction Payment Decoupling, HUD now has a responsibility to preserve and improve its aging stock.[3]

The good news is that *if* HUD does indeed make clear that it will do its part, members of SAHF are willing and able to bring new State and local resources to help HUD satisfy its statutorily provided mission and avoid unnecessary foreclosure and disposition costs. *SAHF members already own and operate nearly 35,000 HUD assisted and insured apartments throughout the Nation.* So long as HUD stands ready and willing to maintain existing Section 8 subsidies, we are able to convince State and local housing providers that their resources are best used in preserving local HUD projects.[4] For example:

- In Anderson, South Carolina, the National Housing Trust/Enterprise Preservation Corporation was asked to rehabilitate a tired, severely undermanaged, drug plagued 200-unit property. The property was one of the only truly affordable housing developments in the somewhat gentrifying area. Once HUD agreed to allow NHT/Enterprise to separate the Interest Reduction Payment from the existing mortgage—a tool that has no budgetary cost whatsoever—NHT/Enterprise was able to secure tax credits and State bonds, and via a deferred developer fee, bring almost $19,000/unit in rehabilitation to the property. NHT/Enterprise also created a community learning center and funded a police substation on site.
- In the State of Missouri, Preservation of Affordable Housing Inc. ("POAH") has, together with the State of Missouri Housing Development Commission, helped to save and revitalize 2,700 HUD-insured apartments located in Independence, Missouri. The new Hawthorne Place Community Center and rehabilitation of Hawthorne Place Apartments will be celebrated with Senator Kit Bond (R–MO) on October 16, 2002. Again, *once HUD agreed to use its Mark-to-Market tool, a tool that has no additional ongoing subsidy cost to HUD, POAH brought new resources totaling $25 million to the properties.*
- In Denver, Colorado, Mercy Housing Southwest, with the Colorado Housing and Finance Authority, city of Denver, Colorado Division of Housing and HUD, preserved 106 units of transitional housing for single parents through the HUD Mark-to-Market Program. The financial restructuring of Decatur Place, built in the early 1980's and home to more than 300 parents and children, created more than $1 million in equity for the rehabilitation of the building. The rehabilitation is almost complete and includes new windows and other significant exterior work, new carpet, and new bathroom and kitchen fixtures and appliances. Without Mark-to-Market, Decatur Place, located in one of Denver's lowest-income neighborhoods, would have continued to operate in substandard conditions. Worse, it might have been foreclosed upon due to the high costs of operation, maintenance, and providing services to its residents. Thanks to the Mark-to-Market Program, other Federal, State, local, and private sources of support were joined together to preserve this important community resource.
- The Subcommittee has already heard testimony from another SAHF member, National Church Residences, and about NCR's important preservation of a HUD property in Manhattan, Kansas.

Photos of some properties saved by members of SAHF are attached as *Exhibit D* to this testimony.[5]

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[3] The most recent example of HUD's lack of perceived preservation responsibility was HUD's failure to protect against the loss of $300 million of Interested Reduction Payment subsidies, funds that could have been used for rehabilitation of HUD properties. *The latest "reinterpretation" of law constitutes another place where HUD is actively or through passivity undermining longstanding preservation policy.*

[4] As we explain below, the Congress must do its part as well. For example, lenders must be assured that current in place, Section 8 subsidies will be renewed.

[5] SAHF's experience in securing tax credits to help rehabilitate HUD-assisted housing is not unusual. In point of fact, State Housing Finance Agencies are increasingly allocating a pref-

Continued

SAHF's Recommendations to the Subcommittee on Preservation of HUD-Assisted Stock

HUD "Reinterpretation" of Section 8 Contracts Upon Refinance of Underlying Mortgage

The Subcommittee has heard a great deal about this issue from the National Council of State Housing Finance Agencies and others. Suffice it to say that SAHF has registered its concern about the subject to Secretary Mel Martinez in a letter dated August 12, 2002, attached as *Exhibit E* to our testimony.

Also attached to this testimony is SAHF's "Top 10 List" of recommendations *(See Exhibit F)* that we believe are essential to help us address the Nation's critical rental housing shortage. Of these, we would like to highlight the following as particularly relevant to the preservation dilemma faced by HUD.[6]

Rights to Distributions

HUD should remove the archaic restrictions on the right of nonprofit sponsors to receive distributions from the operation of affordable housing as long as the distributions are used for affordable housing. In short, HUD should provide a just and reasonable return to nonprofit owners of HUD-assisted and insured housing, to allow them to preserve and produce affordable housing.

For-profit owners may take distributions and profits from HUD-assisted and insured properties for their personal use. Paradoxically, nonprofits often may not take them for charitable purposes. These regulatory and handbook provisions, presumably meant to prevent private "inurement" instead frustrate our ability to support weak projects with strong ones and to develop the capital base for preservation and new development.

Twenty-Year Section 8 Contracts

HUD should provide ready and predictable access to 20-year Mark-Up-to-Market Section 8 contracts, subject to annual appropriations, in connection with nonprofit acquisition and perpetual preservation of affordable housing. Congress has the responsibility of making this clear, either in legislation or report language, so that the financial markets can be assured that these properties can provide a reliable and prudent return on their investment.

In strong markets, in Boston, Massachusetts, Washington, DC, and many parts of California, for example, current owners have powerful economic incentives to convert to market rate use. These are the very communities where the affordable housing cannot be replaced. Even though vouchers protect current tenants, the apartments are eventually lost as affordable housing. Twenty-year Mark-Up-to-Market contracts can enable us to purchase the housing for long-term affordability.[7]

Exit Tax Relief

Although we fully recognize the Senate Subcommittee on Housing and Transportation is not the committee of jurisdiction for tax legislation, we take this occasion to observe that Congress should provide relief from "exit taxes" to those who sell affordable housing to nonprofits for long-term, affordable use.

Because depreciation and other losses have reduced their tax bases, owners of older subsidized housing often would face significant taxes on phantom "gains" but receive no cash if they transfer their properties. As a result, they continue to hold the properties but fail to maintain them. Relief from these exit taxes on noncash

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erence or priority in their tax credit allocation plans for preservation. According to the National Housing Trust, some 30 or more State Housing Finance Agencies prioritize the use of scarcely allocated, very competitively sought tax credits for preservation. There is, of course, no little irony in the fact that the States are taking up the preservation gauntlet while HUD is generally perceived to be somewhat disinterested in the topic. Nevertheless, it is heartening to note that there are important *resources,* resources allocated at the State level, devoted to preservation of HUD assisted housing.

[6] A full set of the SAHF's "Top 10 List" is attached as *Exhibit F* and incorporated herein by reference.

[7] Of course, the members of SAHF believe vouchers are an essential element to provide affordable housing for low-income households. Vouchers are an indispensable element of any affordable housing delivery system. It does not follow, however, that vouchers or certificates are the *only* means to provide suitable housing for poor households. This is not the case for several reasons. First, the voucher may not provide a large enough subsidy to permit the family to stay in the community. Second, in many urban markets, it is difficult for residents to locate and secure 3 or 4 bedroom apartments with vouchers. Also, displaced seniors will have great difficulty using vouchers to access units with meals and support systems. Finally, vouchers appear not to work as well for families facing discriminatory barriers, such as minorities and handicapped individuals. This argues for preserving the housing now as a unique community resource to help serve mixed-income, racially diverse populations.

gains when an owner transfers to a nonprofit would put this irreplaceable housing in the hands of long-term stewards. There are a variety of ways exit tax relief could be implemented: One could permit the noncash gain upon transfer or sale to be nontaxable if the transfer is for $1 plus the outstanding mortgage balance to a qualified, nonprofit purchasers.

Conclusion

Thank you for the opportunity to submit this testimony on the preservation concerns we all share. Now is an appropriate time for us to "rethink" how we preserve good housing stock in decent neighborhoods, housing that serves as a unique resource to communities. We sincerely believe that if HUD becomes a predictable preservation partner, SAHF members and others will bring significantly more resources to help HUD conserve HUD rental housing. SAHF members have created and/or sustained 35,000 HUD-assisted apartments in more than 40 States. We stand ready, willing, and able to do more.