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UNITED STATES GENERAL ACCOUNTING OFFICE

WASHINGTON, D C 20548

RESOURCES AND ECONOMIC DEVELOPMENT DIVISION

JAN 16 1973

Dear Mr Hyde

The General Accounting Office is currently examining into certain aspects of the Department of Housing and Urban Development's (HUD) administration of the urban renewal program.

This review, which is being performed at the HUD headquarters in Washington, D. C , and the regional and area offices in San Francisco and Los Angeles, California, Boston, Massachusetts and Atlanta, Georgia, showed that there are certain weaknesses in HUD's practices in providing funds to local public agencies (LPAs). Such weaknesses, in our opinion, unnecessarily increased the costs of certain urban renewal projects to the Federal Government by about $753,000. Approximately $535,000 of these costs were incurred during the period April 1970 to April 1972 because HUD prematurely made payments to certain LPAs Also, because HUD financed certain projects through direct Federal loans, rather than through LPA loans made on the open market, we estimate that additional costs of about $218,000 were incurred during the period January 1971 to December 1971.

BACKGROUND

Federal financial assistance for urban renewal projects is provided to LPAs either through HUD's direct loans, advances, or grants In addition, HUD guarantees project notes sold on the open market by the LPAs HUD will provide financial assistance to LPAs for two-thirds to three-fourths of the total project costs. The remaining costs are to be provided from local sources by in-kind or cash contributions HUD specifies the amount of loans (direct and open market loans) that it will make or guarantee to financially support the LPAs' projects. This amount represents a ceiling or limit--usually referred to as the amount of loan availability--that is established on LPAs' borrowing authority

The day-to-day working capital needs of LPAs are usually met through open-market sales of federally-guaranteed

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project notes or by direct borrowing from the Federal Government As the project progresses, LPAs receive money from land sales and Federal grant progress payments. This money is designated to retire outstanding loans and notes. HUD may approve the use of these funds as working capital. Funds obtained by LPAs in excess of their immediate financial needs are generally invested in Federal Government securities until such funds are needed.

PREMATURE FEDERAL PAYMENTS TO LPAs

Our work, which included a review of two LPAs in HUD's Region IX, showed that, contrary to HUD's handbook provisions, LPAs received premature payments of about $29.3 million We estimate that for three urban renewal projects (R-54, R-59, and R-122), that were administered by the San Francisco and Oakland Redevelopment Agencies, about $535,000 in additional costs were incurred by the Federal Government because of these payments We examined $29.9 million in funds received by these agencies during the period April 1, 1970, through April 30, 1972, for the three projects. Of this amount, approximately $29 3 million was invested by the LPAs in Federal Government securities for varying periods of time and earned interest income of about $1.2 million.

The following schedule shows an estimate of the additional costs to the Federal Government for these three projects because of premature payments

Estimated costs incurred by Federal Government due to premature payments of $29,331,000 for three Urban Renewal Projects during the period April 1, 1970, to April 30, 1972

Estimated Federal Interest Expense[a]	$1,369,000
Less:	
Federal share of interest income received on LPA's investment of funds	834,000
Net cost	$535,000

[a] The Federal interest was computed on the basis of the monthly average yield on long-term Government bonds Although Federal income tax payments may affect the ultimate costs to the Federal Government, such factors were not included in these computations because LPAs do not pay taxes on income from their investments.

As you are aware, LPAs are required to reduce their project costs by the interest income they receive The Federal Government shares on a two-thirds or three-fourths basis in such income Therefore, we estimate that the Federal Government's share was $834,000 of the interest received by the LPAs. Net costs to the Federal Government because of the above payments amounted to about $535,000.

In September 1972 we discussed with HUD regional office representatives the amounts of funds paid to the agencies for these three projects in excess of their immediate needs and HUD's procedures for the review and control of requests for funds by these agencies These officials said that they do not make any reviews to ascertain whether the requests for funds are in line with LPAs current operating needs and added that they will usually provide funds to LPAs if the funds requested do not exceed 75 percent of the costs of the urban renewal work that has been completed.

LPAs USING DIRECT FEDERAL LOANS INSTEAD OF PRIVATE BORROWING

HUD procedures require that direct Federal loans be made to LPAs only when private borrowing is not feasible. Federal loans, in such cases, are usually made when it is anticipated that the urban renewal project will be closed in the near future (usually within a 3-month period) or when the LPA does not have the authority to borrow funds on the open market.

During our work in the HUD San Francisco Regional Office area, we noted that about $19.5 million in direct Federal loans were outstanding for 12 urban renewal projects as of December 31, 1971

Because HUD did not accurately estimate the length of time that would be required to close certain of these projects, LPAs were permitted to obtain funds by direct Federal loans In addition, contrary to the requirements of the applicable legislation, interest on these loans was not charged by HUD against the LPAs' loan availability. Only the principal was charged

We compared interest costs of 4 of the 12 projects in which the LPAs received about $9 9 million in direct loans from the Federal Government. The additional costs of these projects due to the increased interest costs of obtaining the funds in this manner--not recognizing the effect of income tax receipts by the Federal Government--could amount to about $218,000. The details of our computations showing a comparison in costs between private borrowings and the use of direct Federal loans for these projects for calendar year 1971 are included as appendix I of this report.

Loans Exceeded Loan Availability

As previously mentioned, LPAs' borrowing authority is supposed to be limited to its loan availability amount. In addition, section 102(e) of the Housing Act of 1949 states that, "the total amount of loan contracts outstanding at any one time***shall not exceed the aggregate of the estimated expenditures to be made by local public agencies as part of the gross project cost***." However, under the accounting procedures being followed in Region IX, only the principal was charged against loan availability on direct Federal loans. Interest costs on the direct Federal loans were not charged against such loan availability as is the case in private market loans. If such interest had been recognized, we estimate that as of December 31, 1971, the LPAs' loan availability ceiling on 5 loans would have been exceeded by about $1.5 million. Direct Federal loans, in such cases, circumvented the loan limitations established by HUD.

We discussed this matter with HUD regional office representatives and were advised that they had received no instructions or directions from HUD headquarters requiring that the interest on Federal loans be used to reduce LPAs' loan availability.

Underestimate of Closeout Time

In addition, Federal loans were made for certain projects because HUD determined that the projects would soon be closed and it was not feasible to borrow funds on the open market. For example, we noted that over $4.2 million in Federal funds, acquired through direct loans, were expended over a 12-month period for four projects which, according to HUD officials, were expected to be closed in a relatively short period of time

We discussed these matters with HUD representatives at the regional office and were advised that projects could not be closed until a final audit was completed by the HUD Office of Audit and, in some cases, such audits were not performed when requested

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We recognize that, on several occasions, you have pointed out that additional Federal costs are incurred for urban renewal projects when direct Federal loans, as opposed to private borrowing, are used. Also, the need for HUD field offices to reduce, to the extent possible, outstanding loan balances of LPAs has been identified by HUD in its reviews of urban renewal programs. We believe that based on our work in Region IX, as discussed above, corrective action is needed by HUD to help avoid incurring unnecessary urban renewal project costs

We recommend that you require HUD field offices, in line with the Department's recent decentralization of program responsibilities and authority, to closely monitor payments to LPAs. In this regard, we recommend that LPAs be requested to provide HUD with periodic cash forecasts in support of their requests for payments. Such forecasts should identify the amount of funds that LPAs expect to use for the repayment of outstanding loans and also the amount of funds needed for current operating expenses.

With respect to the use of direct Federal loans as opposed to private borrowing, we recommend that you issue instructions to HUD field offices requiring that they recognize the full amount of Federal loan obligations (principal and interest) in reducing the loan availability of LPAs

Furthermore, HUD field offices should be required to critically examine the information that is submitted by LPAs in support of their requests for direct Federal loans to finance their projects on the basis that the projects will soon be closed and borrowing funds on the open market is not feasible

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We would appreciate receiving, within 30 days, your comments on any action taken or planned on the above matters. If you have any questions or wish to discuss the above information, we would be pleased to meet with you or members of your staff.

A copy of this report is being sent to the HUD Inspector General.

Sincerely yours,

B. E. Birkle

B E Birkle
Associate Director

The Honorable Floyd Hyde
Assistant Secretary for
Community Development
Department of Housing and
Urban Development

COMPARISON IN COSTS BETWEEN FEDERAL LOANS AND PRIVATE BORROWING ON FOUR URBAN RENEWAL PROJECTS JANUARY 1, 1971 TO DECEMBER 31, 1971

Line item	Description	Projects R-8	R-10	R-37	R-44	Total
1	Federal loans	$1,320,000	$805,665	$4,783,823	$3,038,638	$9,948,126
2	Federal Interest[a/]	84,136	51,353	304,920	182,287	622,696
3	Estimated private market interest (2 97% of line 1)[b/]	39,204	23,928	142,080	90,248	295,460
4	Additional project costs due to Federal loans (line 2 less 3)	44,932	27,425	162,840	92,039	327,236
5	Federal share (2/3 or 3/4 of line item 4)	29,955	18,283	108,560	61,359	218,157

a/Federal interest on long term Government bonds during 1971 varied between 5 7/8 to 6 1/2 percent.

b/Private interest rate (2.97%) based on average rate paid for 1 year project notes in Region IX during January 1971

BEST DOCUMENT AVAILABLE