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Testimony

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HOUSING AND URBAN  
DEVELOPMENT

Management and Budget  
Issues in HUD's  
Fiscal Year 1995  
Appropriation

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Mr. Chairman and Members of the Subcommittee:

We are pleased to offer GAO's analysis and comments as part of the fiscal year 1995 appropriations hearing for the Department of Housing and Urban Development (HUD). Faced with increasingly limited budgets and seemingly limitless demand for its resources, HUD is scrutinizing the way it operates so that it can do more with less. HUD's effort is two-pronged: The Department is totally reorganizing to improve the delivery of its services at the same time that it is "reinventing" itself--examining the emphasis of its programs, its priorities, and its way of doing business. The outcome of these efforts--how HUD organizes itself and designs, implements, manages its programs--will have a substantial effect on the appropriations it seeks.

In summary, on the basis of recently completed or ongoing work for several different committees, we have identified a number of issues in need of further study or resolution in HUD's management of either specific programs or significant portions of its budget.

#### Program Management Issues

- Efforts to reinvent HUD present several challenges, including trying to change an organizational culture that has become reactive and defensive, a potential for the overall reorganization of the Department to overshadow the reinvention initiatives, and the possibility that available resources may not be adequate to complete HUD's ambitious agenda.
- The Government National Mortgage Corporation (GNMA), an agency within HUD, continues to be subject to the staffing limitations applied to the Department as a whole. As a result, GNMA may be unable to focus on areas of risk and exposure to the extent it should and may experience difficulties in responding to future management challenges.
- HUD continues to be plagued by lack of information and by information security problems because its information systems have not been planned and managed to serve its missions and meet its strategic objectives. While HUD's management has identified corrective actions, the problems will take years and sustained management commitment to correct.

#### Budget Management Issues

- HUD routinely carries forward from year to year substantial balances of unobligated funds--\$33.2 billion at the close of fiscal year 1993, for example. While most of these funds are earmarked for specific accounts or "reserved" for programs, the remaining carryover amounts--\$2.2 billion in fiscal year 1994--are sufficient to raise questions about the ability of

the Department to spend its funding efficiently and its need for new budget authority.

- HUD has a backlog of at least \$1.4 billion in funds appropriated, obligated, and approved for use by public housing authorities (PHA) for modernizing public housing, but not yet in use. Additional funds amounting to \$7.9 billion, including HUD's fiscal year 1994 appropriation, are also not being used, because either HUD or the PHAs has not yet obligated them.
- HUD has not been able to accurately estimate the future costs of incentives it provides to property owners to preserve their properties as low-income housing. This difficulty is a result of the inherent uncertainty in predicting whether property owners will file for preservation incentives, and if so, when they will file.
- Given its recent experience with the New Orleans PHA, HUD could have some responsibility to help settle claims currently being filed against PHAs and private landlords as a result of lead-based paint poisoning.

Our work in several of these areas is continuing, and we will report our findings to the Congress later this year and early next year. Although the focus of this hearing is HUD's budget request for fiscal year 1995, the issues we discuss in this statement do not lend themselves to solutions HUD could realistically implement in a single year. As a result, HUD's efforts to address any one of these issues cannot be assessed in isolation, but rather as part of a multiyear effort to manage its funds and programs to better serve its customers. We fully expect--and view it as no criticism of HUD--that we will again speak to these issues in subsequent years.

I would now like to turn to the specific issues at hand today.

#### REINVENTING HUD

We laud Secretary Cisneros and his management team for the energetic and active leadership they have demonstrated in trying to reinvent HUD. Few would question that the Secretary inherited an agency sorely in need of change and that transforming the agency is a serious challenge.

Secretary Cisneros initiated the reinvention of HUD shortly after assuming office. The principal activities in this effort include:

- consulting with HUD employees and customers to identify impediments to the achievement of departmental objectives and recommendations for overcoming these impediments;

- forging new partnerships between HUD's management and the union and between HUD and the communities it serves;
- entering into a performance agreement with the President that establishes time-specific, quantifiable standards for measuring performance and developing work measurement indicators for each program office; and,
- reorganizing the agency so that it becomes more results-driven and customer-oriented.

It is premature to evaluate the success of the reinvention effort or even to determine if HUD is reinventable. HUD faces monumental challenges, the most basic of which is trying to change an organizational culture that has become reactive and defensive.

While some of HUD's challenges can be tackled internally, others are subject to external constraints. Congress and the administration must provide the flexibility HUD needs to become a responsive and accountable public institution. HUD, the Administration, and the Congress will need to work together to institutionalize the Secretary's plan for change. That is, changes made should not be limited to a short-term turnaround; they will need to be sustained beyond the Cisneros administration and become assimilated into HUD's routine processes.

#### Changes in Program Management Challenge HUD

While monitoring HUD's reinvention efforts, we observed some potential problems. First, HUD's reorganization may be overshadowing other reinvention activities. Initially, HUD identified, through employee and customer consultations, thousands of recommendations for improved delivery of its programs. However, HUD employees have told us that reinvention efforts have been directed away from implementation of these recommendations and toward the reorganization.

Second, HUD has embarked upon an ambitious, but possibly unachievable, reinvention agenda. Given budgetary constraints, HUD is not likely to receive the level of funding it has requested and therefore may not be able to implement all its agenda items.

For example, the agency is analyzing its workload, anticipating moving staff to areas where a greater demand for HUD services exists. Yet, with moving costs estimated at \$50,000 per employee, HUD may encounter difficulty in covering relocation costs. Further, if staff are unwilling to move, the agency's staffing-demand imbalance will not be remedied.

Another example of a reinvention initiative which HUD may not be able to completely implement involves training. HUD has established a training academy to improve the delivery of training

to HUD employees. The academy is operational, offering courses such as change-management training. But, again, unless the agency receives increased resources or finds ways to use its current resources more effectively, it may be unable to implement all the training enhancements it envisions.

GNMA NEEDS GREATER STAFFING  
FLEXIBILITY TO IMPROVE MANAGEMENT

In our June 1993 report, we pointed out that despite GNMA's status as a revenue-generating, government-owned corporation and despite the large federal liability inherent in its operations--\$426 billion--GNMA's managers have limited authority to add personnel to manage their assets. GNMA does, however, have the flexibility to retain contractors, who now perform virtually all of GNMA's administrative and management information functions. While contractors are needed, GNMA must have a sufficient number of staff to properly manage and be accountable for its work. However, a HUD staffing study concluded that GNMA does not have sufficient staff to properly manage its work load.

We concluded that GNMA's staffing needs have to be considered apart from HUD's personnel limitations because providing additional staff to GNMA by reducing staffing levels elsewhere in HUD would add to problems reported by HUD's Office of Inspector General, which said that HUD has insufficient staff to perform necessary functions. We concluded that if GNMA's staffing needs continue to be tied to HUD's personnel ceilings, the agency may not be able to focus its attention on areas of risk and exposure to the extent that it should and may have difficulty responding to future management challenges. Moreover, we concluded that GNMA could experience difficulties competing in a changing secondary mortgage market. For example, GNMA would like to take advantage of new opportunities to benefit low-and moderate-income home buyers by offering to guarantee a potentially profitable investment security called a Real Estate Mortgage Investment Conduit (REMIC). However, HUD was concerned that GNMA did not have the in-house expertise or staff to manage such a program.

To ensure that GNMA has the flexibility to manage its growing work load, respond to changing markets, and create new products, we recommended that the Secretary of HUD and the Director, Office of Management and Budget (OMB), work together to consider GNMA's staffing needs and provide for those needs without regard to personnel limitations imposed on HUD. We further recommended that the Secretary report to the Congress within 60 days of the issuance of our report on the options that it and OMB considered and the actions they took to provide GNMA with the resources it needs to operate in a business like manner while reducing the overall financial risk to the federal government. We also pointed out that the Congress should monitor HUD's and OMB's efforts to resolve GNMA's staffing problems. If the agencies do not resolve this

problem, we suggested the Congress may wish to consider directing OMB and HUD to provide GNMA with the necessary staff without regard to HUD's personnel budget.

HUD and GNMA agreed with the thrust of the conclusions and recommendations in our report. OMB agreed to review GNMA's staffing situation, but cautioned that its review would, at a minimum, consider GNMA's staffing situation in the context of the financial and other program implementation risks posed by GNMA relative to other HUD programs. Given OMB's position, we noted in our final report that it is unclear what steps OMB would take in addition to what has been done in the past. Therefore, we concluded that it was important that the Congress look carefully at HUD's report on how GNMA's staffing problems will be resolved.

In response to our report, the Secretary of HUD, in a February 3, 1994 letter to the appropriate congressional committees, stated that one of the first priorities of GNMA's president is to explore ways to provide sufficient staff to carry out GNMA functions. As of the time of this testimony, HUD and OMB had not submitted a written statement on the actions taken on our recommendations. However, HUD has announced that GNMA would begin developing and managing a REMIC program in fiscal year 1994 and requested additional staff to do this. GNMA expects to begin marketing REMICs shortly.

#### PLANNING AND USE OF INFORMATION RESOURCES NEED TO BE IMPROVED

HUD relies on information systems to help it administer federal housing programs, enforce fair housing, and improve the nation's communities. But, the Department has been plagued for many years by information systems that do not satisfy management needs or provide adequate control.

This condition persists because HUD's plans for information resources management have not been based on strategic business plans that articulate what senior executives expect to accomplish and what strategies, processes, resources, and information are needed to achieve departmental missions and objectives. Furthermore, HUD has not

- developed a departmentwide information architecture so that there is a standard framework for governing the management and use of information and resources,
- developed a data management program to ensure that departmentwide systems provide managers with the information they need to effectively accomplish their missions,
- established adequate computer security controls for systems that process sensitive and privacy data, or

-- provided for the recovery and continued processing of critical systems in the event of a major disruption or disaster.

HUD's effort to develop and implement an integrated financial system has also been impeded by ineffective planning and management oversight. Collectively, these problems threaten HUD's ability to provide information and effectively use information resources to fully support the Department's future directions, missions, priorities, and programmatic needs.

Senior managers told us they recognize the need to correct these problems and said the Secretary is committed to developing a strategic business plan. In addition, the Department has initiated actions and plans to address the weaknesses in planning and oversight of data management, computer security, and financial systems integration.

The Secretary's commitment to strategic planning and HUD's early steps to address strategic planning represent the first substantive actions since GAO reported on the absence of strategic information resource planning a decade ago. This commitment and HUD's initial efforts to address the other information management problems we identified are encouraging. Fully correcting these problems will require the sustained attention and commitment of the Department's leadership and managers over a number of years.

UNOBLIGATED BALANCES ARE BEING CARRIED FORWARD FROM PRIOR FISCAL YEARS

HUD's budget request shows that the Department carried forward \$33.2 billion in prior fiscal years' unobligated funds at the end of fiscal year 1993. This amount exceeded HUD's total annual budget for that year of \$26.5 billion.<sup>1</sup> Over half of the Department's unobligated funds (\$19.6 billion) were appropriated for its Annual Contributions for Assisted Housing account, which funds programs such as public and Indian housing modernization, amendments to Section 8 contracts, and lead-based paint abatement.

Of the unobligated funds remaining in the Annual Contributions account, HUD has administratively reserved nearly 90 percent, or

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<sup>1</sup>In the federal budget process, balances of funds in budget accounts are generally described as obligated, unobligated, or unexpended. Obligated funds are those for which an agency has placed orders, awarded contracts, or made similar transactions and for which payment has not been made. Unobligated funds are those that have not yet been used for such transactions and for which an agency or the federal government has made no binding agreement; unexpended funds consist of both obligated and unobligated funds that have not been disbursed.



\$17.4 billion, for specific projects, contracts, or programs.<sup>2</sup> (HUD carried over \$2.2 billion for use during the current fiscal year, 1994, that was neither reserved nor obligated during fiscal year 1993). Not all projects for which HUD reserves funds ultimately result in obligations and expenditures. For a variety of reasons, projects can be cancelled or deemed by HUD to be no longer feasible. In these cases, HUD recaptures the funds. Unless directed to do otherwise by the Congress, HUD uses recaptured funds for the same programs for which they were originally reserved.

In budget justification documents for several recent fiscal years, HUD has shown its current estimate of the reserved funds it expects to recapture that year. For example, in the justification for its fiscal year 1994 budget request, HUD estimated it would recapture \$242.7 million. Added to its new request for that year of \$8.4 billion, this gave HUD an estimated total budget authority for the Annual Contributions account of \$8.7 billion. HUD's budget summary for fiscal year 1995 shows no estimated recaptures as part of its total request for budget for this account.

#### SOME MODERNIZATION FUNDING IS BACKLOGGED

As of September 30, 1993, HUD had a backlog of \$1.4 billion in modernization funds for public housing. HUD considers these funds backlogged if more than 2 years have passed since it obligated them for use by PHAs and the PHAs have failed to either use the funds themselves or enter into a contract to have the modernization work performed.<sup>3</sup>

An additional \$4.9 billion has been obligated by HUD for use by the PHAs within the last two years but has not yet been obligated by PHAs, and thus is not considered part of the backlog. HUD has yet to obligate any of its 3 billion-dollar fiscal year

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<sup>2</sup>HUD uses administrative reservations (also called "commitments") as budget tools to account for funds between its initial appropriation and the time it obligates funds for individual programs or projects. Using these tools, HUD can give grantees, such as PHAs, the go-ahead to initiate work required before HUD formally approves the funding.

<sup>3</sup>The term "obligated" is used twice when describing public housing modernization funds. Both HUD and individual PHAs obligate these funds, but at different stages in the budget process. HUD's obligation comes first--when it approves a PHA's proposed use of the funds. The PHA's obligation occurs when the PHA the funds itself for modernization work or enters into a binding agreement for a contractor to perform the work.

1994 appropriation for its two major modernization programs,<sup>4</sup> and thus the funds are still not available for the PHAs to begin to place under contract.

Both HUD and the PHAs for which it approves funds share responsibility for funds remaining backlogged. Some PHAs have experienced delays in awarding contracts for modernization work because they did not develop the architectural and engineering plans HUD requires until after HUD made the modernization funds available. While it is possible a PHA could complete these plans concurrent with HUD's review of its application, most are hesitant to do so prior to getting HUD's approval for the project.

Other PHAs, as HUD requires, had to test for and eliminate asbestos and lead-based paint in housing units before proceeding with the modernization work. Some PHAs also lacked technical skills needed to efficiently manage large modernization efforts to HUD's satisfaction, or were required to go through multiple levels of local review before they could award contracts.

HUD and a number of PHAs have been directing efforts specifically aimed at reducing the \$1.4 billion backlog. HUD has provided additional guidance to PHAs for administering modernization projects and has streamlined some procurement requirements. In addition, HUD officials have placed greater emphasis on the backlog by requiring PHAs to provide more financial information that can help HUD monitor obligations more closely. Also, some PHAs have hired construction management firms to manage projects and provide the expertise they did not or could not provide themselves.

#### FUTURE COSTS OF PRESERVATION INCENTIVES REMAIN UNCERTAIN

The owners of certain multifamily housing projects developed with government assistance during the 1960s and 1970s are eligible to prepay their mortgage after 20 years. Prepayment could result in the termination of federal restrictions on the way the properties can be used that are designed to maintain this housing for lower-income households. Faced with the threat of losing a large number of housing units as a result, the Congress enacted legislation in 1987 and 1990 to provide owners with incentives to preserve this housing; that is, to keep it available to lower-income households.

By the end of fiscal year 1994, almost 3,300 projects containing over 351,000 units will be eligible for preservation incentives that generally take the form of additional Section 8

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<sup>4</sup>The Comprehensive Improvement Assistance Program and the Comprehensive Grant Program.

subsidies.<sup>5</sup> These units represent about 90 percent of the total units eligible for preservation incentives. However, through fiscal year 1993, only 132 projects, containing 19,810 units, have been approved by HUD for preservation. The estimated cost to preserve these units is \$432 million.<sup>6</sup>

Because of the discretion afforded owners to file for the incentives, HUD's task of estimating preservation costs and the Congress's task of budgeting for future years' appropriations are difficult. Nevertheless, because the overwhelming number of project owners that could potentially apply for preservation incentives, the future impact of this program on HUD's budget is uncertain.

To estimate this budgetary impact, HUD has developed a model that projects costs on a yearly basis. Initial estimates from the model were too high in the early years because of assumptions that owners would apply for incentives as soon as they were eligible. The additional funds requested as a result contributed to a significant carryover in appropriated funds that have not been reserved.<sup>7</sup> HUD has refined the model in an effort to improve future estimates. However, the continued uncertainty of when owners file for preservation incentives, as well as the costs of these incentives as they relate to particular projects, will continue to hinder HUD's efforts to accurately estimate the funds it will need.

#### HUD NEEDS TO ACT ON OUR EARLIER LEAD-BASED PAINT RECOMMENDATIONS

According to the National Center for Lead-Safe Housing, childhood lead poisoning is the number one environmental health hazard facing American children. The National Center cites federal estimates that 10 to 15 percent of all preschoolers--as many as 3 million--have blood lead levels high enough to warrant concern for

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<sup>5</sup>HUD's Section 8 rental assistance program provides housing subsidies that allow lower-income households to obtain decent and affordable housing.

<sup>6</sup>At the end of fiscal year 1993, 10 of the 132 projects approved for preservation had not had funds reserved for them because, according to HUD's Preservation Office staff, unresolved questions remained between HUD and the owners over the final incentive packages. All but one have had funds reserved for them since the end of fiscal year 1993. The remaining project received an incentive that did not require funding to be reserved.

<sup>7</sup>From 1991 through fiscal year 1993, \$1.1 billion was appropriated while only \$432 million was actually reserved.

their intellectual development. At least 700,000 children live in the 5 million federally assisted residences nationwide, many of which were constructed before the use of lead-based paint was banned in 1978 and may have not been substantially renovated to remove lead-based paint. Although the overriding goal of federal housing assistance is to provide decent, safe, and sanitary housing to low-income families, the presence of lead-based paint in this housing threatens that goal because it threatens the health of families and their young children that live there.

Until October 1993, public housing authorities were able to participate in a "master insurance policy" managed by HUD that insured the housing authorities and their contractors against the risks of being sued for damages that occurred during lead-based paint abatement activities. Likewise, until recently, private property owners, many of whom participate in HUD's section 8 assisted housing programs, were protected against the threat of law suits by their standard property insurance. However, for many reasons, including the belief that insurance for public housing authorities was becoming more widely available, HUD did not renew the master policy when it expired in October 1993. Although insurance is still available in many parts of the country, the industry as a whole is moving to restrict coverage for lead-based paint hazards, particularly in areas of the country with substantial amounts of older, low-income housing.

Lawsuits on behalf of children who have been lead-poisoned have been brought against housing authorities in Baltimore, MD, Chicago, IL, and New Orleans, LA. Without insurance, housing authorities and property owners are left to either self-insure or remove the lead-based paint from their dwellings. Either choice can be expensive. According to the National Center for Lead-Safe Housing, the cost of full abatement of all lead-based paint can range from \$7,500 to \$40,000 per unit. And jury awards for damages have reached as much as \$2,000,000.

Although to our knowledge HUD is not currently named in any suits, in at least one case the Department has already shared in the costs of litigation and the resulting settlements that were not covered by insurance. In 1991, the New Orleans Housing Authority settled over 60 lawsuits arising from lead poisoning that cost the authority over \$1 million in claims and attorneys' fees. HUD provided \$340,000 to help defray the costs of these claims. Notwithstanding this settlement, HUD's Assistant Secretary for Public and Indian Housing told us that he sees no legal liability in the longterm for the Department, although he questions who eventually will pay for the damages suffered as a result of lead poisoning.

PHAs, already heavily dependent on HUD for funding to operate, may have to seek HUD's help to defray the costs associated with these lawsuits. To minimize lead-based hazards and the risks of

being sued, HUD should act on recommendations we have made in the past regarding better communication with public health agencies and enforcement of lead-based paint regulations in federally assisted housing.

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In conclusion, as this Subcommittee as well as the full Appropriations Committee assist HUD in meeting the challenges before it, we would like to reiterate that we see promise in HUD's reinvention efforts to date as well as a number of potential stumbling blocks that can impede its success. Foresight and planning will be needed to capitalize on today's innovations while avoiding tomorrow's obstacles.



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