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GAO

Report to the Chairman, Special Committee on Aging United States Senate

September 1986

# HOUSING FOR THE ELDERLY

# HUD's Cost Containment Program Could Be More Effective

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GAO

**United States**
**General Accounting Office**
**Washington, D.C. 20548**

**Resources, Community, and**
**Economic Development Division**

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September 9, 1986

The Honorable John Heinz
Chairman, Special
Committee on Aging
United States Senate

Dear Mr. Chairman:

In response to your request, this report describes what the Department of Housing and Urban Development's cost containment initiatives have accomplished in reducing costs in the section 202 elderly housing program. It discusses the problems the Department has encountered in administering these initiatives, as well as additional opportunities for further reducing program costs. In addition, it describes the demographic, financial, and housing characteristics of the elderly being served by the section 202 program.

As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of the report. At that time we will send copies to interested parties and make copies available to others upon request.

Sincerely yours,

Neal P. Curtin

for J. Dexter Peach
Assistant Comptroller General

# Executive Summary

Over 4 million very low-income elderly people have a need for housing assistance. In fiscal year 1985, the Department of Housing and Urban Development (HUD) provided $600 million in subsidized construction loans and $1.7 billion in rent subsidies to provide 12,400 housing units primarily for the elderly. At the request of the Senate Special Committee on Aging, GAO

- reviewed how well HUD initiatives to control program costs were working,
- assessed whether additional opportunities existed for controlling costs further, and
- identified who was benefiting from the program.

## Background

Under section 202 of the Housing Act of 1959, as amended, HUD makes reduced-interest rate loans to nonprofit entities, or sponsors, to construct housing for the elderly. Since 1974, this loan program has been used in conjunction with HUD's section 8 rental assistance program. This program provides subsidies to cover the difference between the amount the tenant pays (30 percent of income) and the rent for the unit.

HUD controls project construction costs through modest design requirements it issued in 1981. These requirements state that 25-percent of the projects are to be comprised of efficiency units and limit the size of units, amenities, and commercial space included in projects. In 1983 HUD issued supplemental guidelines to further eliminate costly features from projects. HUD also controls the construction costs of housing units for the elderly by limiting project rents to no more than 120 percent of fair market rent (a composite of rents for comparable units in the immediate area). (See pp. 10 and 18.)

## Results in Brief

GAO found that projects built under HUD's cost containment initiatives are more modest and have unit costs that average 16 percent (inflation adjusted) less than the projects built before HUD's initiatives were implemented. Without this cost reduction, GAO estimates that HUD would have required about $100 million more to fund the 12,400 section 202 units approved in fiscal year 1985. (See p. 18.)

However, cost reductions were not fully realized because (1) HUD guidelines do not specify that the supplemental cost containment provisions are to be applied to all projects, (2) HUD's project selection process does not always select the project with the most modest design, and (3) sponsors have generally not increased the number of less costly efficiency units in projects beyond those required under cost containment. (See pp. 18 and 34.)

Most program beneficiaries were single and had very low incomes. Minorities, however, benefited less from the program than nonminorities relative to their respective need for housing assistance. (See p. 50.)

## Principal Findings

### Effect of Cost Containment

GAO analyzed nationwide cost data for 802 section 202 projects approved after January 1, 1980, and found that cost containment projects had on average 11 percent less space, more efficiencies, and fewer amenities than those constructed before cost containment. In addition, GAO reviewed 85 projects at 10 HUD offices and found that cost containment projects had loans that averaged 9 to 25 percent less per unit than precost containment projects. This reduced project rents an average of 10 percent.

According to HUD officials, the supplemental cost containment guidelines were intended to apply to all projects. But HUD's guidelines allowed exceptions when project rents were 100 percent or less of fair market rents. For example, one three-story project in Boston was allowed to have three elevators because its rents did not exceed 100 percent of the fair market rent. If HUD guidelines had been applied, which would have limited this project to one or two elevators, construction costs would have been reduced. In April 1986, HUD directed its field offices to apply the guidelines to all projects. (See p. 25.)

### Opportunities for Reducing Costs

Program costs could be further reduced by housing more single elderly people in efficiency units. Currently, over 80 percent of the tenants served by the program are single. Most single elderly people live in one-bedroom units even though HUD considers efficiency units the most appropriate housing for such tenants.

According to several HUD officials, sponsors have been reluctant to include efficiencies in their projects because fair market rents for these units are usually less than the rents needed to construct and operate them. This occurs because fair market rents are based on a sample of rents from an area's private market rents. Efficiencies, however, are an anomaly in the private market. They are included in projects to utilize space that otherwise would not be used. Consequently, rents for these units generally do not cover average total costs.

Some sponsors also said that efficiencies are more difficult to market because the units are small and lack privacy. However, better designed efficiency units, such as those used by some sponsors, can provide greater privacy, thereby enhancing their marketability.

To facilitate the construction of more efficiencies, HUD could adjust the rents for efficiencies to better reflect their construction and operating costs. GAO estimates that if 80 percent rather than 25 percent of the units HUD financed in fiscal year 1985 had been efficiencies, program construction costs could have been reduced by about $19 million—enough to build about 400 more units. (See p. 36.)

HUD's ranking system places a greater emphasis on a sponsor's financial and operational capability, and does not always result in selecting projects with the most modest design. HUD could utilize a two-tiered system that first identifies all sponsors with acceptable financial and operational capability and from them select the ones with the most modest design. GAO found that under such a system, HUD could have selected projects that were not only financially and operationally sound, but may have resulted in further reduced costs because of their more modest design. (See p. 40.)

## Program Beneficiaries

Tenants in the projects GAO sampled were mostly single, had on average an annual income of $6,600, paid $146 monthly for rent, and received $334 in monthly rent subsidies. Over 80 percent had incomes of 50 percent or less of the area's median income (family size adjusted).

Minorities, which represent 22 percent of the elderly in need of housing assistance, accounted for 13 percent of the tenants sampled. Most projects sampled had few or no minorities—most minorities lived in a small number of projects.

HUD is in the process of strengthening its civil rights monitoring and enforcement efforts. (See pp. 50 to 64.)

## Recommendations

GAO recommends that the Secretary of Housing and Urban Development:

- Adjust rents for efficiency units to make these units more financially feasible for sponsors to construct and operate. (See p. 48.)
- Increase the importance of modest design in HUD's project selection process. (See p. 48.)

GAO makes additional recommendations to HUD to increase monitoring of cost containment requirements and reexamine whether its policy of waiving its efficiency requirement should be continued. (See p. 32.)

## Agency Comments

HUD stated that it has been studying various ways to address the financial feasibility issue regarding building efficiencies and will continue to do so, but disagreed that rents for these units should reflect the costs to construct and operate them. HUD also stated that GAO's proposal could lead to inflated costs. GAO's work shows that in some cases, HUD needs to bring fair market rents more in line with the costs to construct and operate efficiency units. Such an adjustment would make these units more financially feasible for sponsors to build. HUD also can use the cost containment methods discussed in this report to prevent inflated costs. GAO's recommendation does not specify how rents should be adjusted but rather leaves this decision to HUD's discretion.

HUD considers its current selection process adequate to make informed decisions and disagrees that increasing modest design's importance in project selection would save money.

GAO believes that if HUD first identifies sponsors with acceptable financial and operational capability and from them selects projects with the most modest design, cost reductions, although difficult to quantify, could be achieved. (See p. 46.)

HUD plans to rescind field office authority to grant efficiency waivers but believes its current ongoing monitoring efforts are adequate. (See p. 31.)

# Contents

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## Tables



## Figures

## Abbreviations

| | |
|---|---|
| GAO | General Accounting Office |
| HUD | Department of Housing and Urban Development |
| FMR | fair market rent |

# Introduction

Several million households headed by elderly persons with limited incomes need government assistance to obtain decent and affordable housing. The Department of Housing and Urban Development's (HUD's) section 202 program is the primary means of federal assistance available to provide new housing units to help meet this need.

## HUD's Section 202 Elderly Housing Program

HUD's elderly housing program was authorized by section 202 of the Housing Act of 1959 (12 U.S.C. 1701q). Under this program, HUD makes direct loans to nonprofit organizations (sponsors) to construct or rehabilitate rental housing for the elderly and handicapped. Throughout fiscal years 1984 and 1985, loans had an interest rate of 9.25 percent and were repayable in terms of up to 40 years. Projects are to be designed to provide an independent living environment, including provisions for necessary services, such as health, continuing education, welfare, recreation, and transportation. Projects also can include essential service facilities, such as dining facilities and multipurpose community rooms.

The Housing and Community Development Act of 1974 permits HUD to use the section 202 program in conjunction with the section 8 rental housing assistance program established by this act. The section 8 program authorized HUD to make rental assistance payments on behalf of lower income families (households) to enable them to obtain decent and affordable housing. The section 8 new construction phase of the program authorized HUD to contract to make assistance payments for 20 years to owners that constructed new housing units for low-income families. Low-income families are defined as those with incomes not exceeding 80 percent of the median income (adjusted for household size) for their particular area of residence. However, based on subsequent amendments, eligibility is generally restricted to families with very low incomes—those that do not exceed 50 percent of the median income for the area.

Families eligible for assistance generally are required to pay 30 percent of their income (after allowances) for rent. The section 8 assistance payment covers the difference between the amount the tenant pays and the rent for the unit. Project (contract) rents are limited to those necessary to operate and maintain the project and to cover financing of loans incurred to develop/construct the project. Project rents, however, cannot exceed 120 percent of the fair market rents (FMRs) established annually by HUD for each housing area on the basis of rents for comparable units. In authorizing HUD to approve project rents up to 120 percent of FMRs, the Congress anticipated that this authority would be used only in exceptional cases, according to the House and Senate conference committee report on the 1974 Act. This control on rents limits the mortgage financing that sponsors can obtain for project construction costs.

The FMRs for new construction include utilities, except telephone; ranges and refrigerators; and all maintenance, management, and other services required to obtain privately developed, newly constructed rental housing of a modest (nonluxury) nature. Separate FMRs have been established for units with different numbers of bedrooms, for various types of projects (e.g., detached, semidetached), and for different housing market areas. FMRs for section 202 projects include an additional 5 percent to cover the special housing needs of the elderly, such as emergency call buttons and grab bars.

## Mechanics of the Section 202 Program

Before construction of a section 202 housing project can begin, HUD requires sponsors to go through a series of processing stages. These stages (see app. I) include requirements designed to ensure that the proposed project (1) is eligible for a section 202 loan and rent subsidy assistance under section 8, (2) serves programmatic goals, (3) is well-designed but modest, (4) has a sufficient and reasonable construction budget, and (5) has rents that are in line with section 8 rent limits and are adequate to support project management, maintenance, and debt service.

The three major processing stages for section 202 loans are initial selection, conditional commitment, and firm commitment. At the initial selection stage, potential sponsors respond to a HUD invitation, which generally identifies how many section 202 units will be funded and which locations will receive priority. Applications describe the prospective sponsor, identify a proposed site, sketch the project layout and design, and describe the services to be provided to tenants. HUD field office staff evaluate applications by rating the potential sponsor's financial and managerial capacities, the site location, the project design, and the extent of tenant displacement.

The projects selected for funding no longer have to compete with other projects for participation in the section 202 program. Generally, project selections are completed late in the fiscal year—in August or September. Projects then begin the process of obtaining HUD approval of detailed plans and budgets, which typically takes a year to complete.

Conditional commitment and firm commitment processing are similar in most respects. A sponsor submits preliminary plans and specifications, obtains HUD's general approval (subject to specific conditions), and then submits final plans and specifications to obtain a firm commitment. Thus, conditional commitment and firm commitment can be viewed as two runs through a common set of requirements. In both conditional and firm commitment processing, projects are analyzed by five technical specialties—architecture and engineering, cost, valuation, mortgage credit, and housing management.

According to HUD, the conditional commitment phase is critical because it provides HUD with the first real opportunity to review project design before considerable moneys are expended for the preparation of final plans and specifications. HUD stated that it is often able to require design changes that would produce cost savings that could not otherwise be realized at a later stage of processing. In addition, the conditional commitment stage is the first point where HUD can develop its cost estimate. This estimate allows HUD to determine whether the project will be feasible within the allowed budget.

## Program Successes and Problems

Section 202 has historically been a successful and popular program. The projects financed have had few management problems and almost no defaults, and have provided quality housing for which there is considerable demand. Recently, however, the program's high cost, its impact on the federal budget, and the incomes of the tenants served have caused legislative and executive concerns. In response to these concerns, the Congress and HUD took actions to limit program growth (see table 1.1) and to target assistance to very low-income families.

**Table 1.1: Section 202/8 Funding**

Dollars in Millions

| Fiscal year | Units | Section 202 loans reserved | Section 8 budget authority |
|---|---|---|---|
| 1981 | 15,200 | $870 | $1,920 |
| 1982 | 16,000 | 820 | 2,000 |
| 1983 | 14,300 | 630 | 1,840 |
| 1984 | 14,300 | 670 | 1,900 |
| 1985 | 12,400[a] | 600 | 1,700 |

[a]Does not include 200 units approved in prior years which require additional funds.

In March 1981, we issued a report, How to House More People at Lower Costs Under the Section 8 New Construction Program (CED-81-54, Mar. 6, 1981). That report discussed how the section 8 program could be made more efficient. Specifically, we reported on how

- the sizes of the units were significantly larger than the minimum size considered adequate using HUD's minimum property standards;
- single elderly persons could be housed in efficiency units rather than one-bedroom units; and
- amenities, such as balconies, could be eliminated.

Similarly, HUD reported that the average unit cost of a section 202/8 unit ($33,537 in 1980 dollars) was about 12 percent more than the cost of an unsubsidized, HUD-insured unit.[1]

To help improve this situation, the Housing and Community Development Amendments of 1981 (P.L. 97-35, 95 Stat. 384) directed HUD to assure that newly constructed housing assisted under section 8 is modest in design. According to the House/Senate conference report on these amendments, HUD was to preclude unnecessary amenities, reduce room sizes where possible, and encourage an appropriate mix of efficiency and one or more bedroom units. The report further stated that projects should not be required to have more than 25 percent of their units as efficiencies. This limitation was eventually incorporated into the section 202 program through amendments made by the Housing and Urban-Rural Recovery Act of 1983 (12 U.S.C. 1701q(i)(1)).

In November 1981, HUD issued a series of cost containment and modest design requirements to help reduce the cost of section 202 projects. These requirements and their effects on project costs are discussed in chapter 2. To further contain cost, HUD management plans for its field offices provide that at least 10 percent of projects for the elderly have rents of 100 percent or less of fair market rents.

## Objectives, Scope, and Methodology

In June 1984, we began a review of HUD's section 202 elderly housing program at the request of the Chairman, Senate Special Committee on Aging. On the basis of our preliminary review and subsequent meetings with the Committee, we agreed in September 1984 to examine and report on

[1]U.S. Department of Housing and Urban Development, The Costs of HUD Multifamily Housing Programs. (Washington, D.C.: U.S. Government Printing Office, 1982).

- the extent to which HUD's cost containment requirements were working,
- additional opportunities for reducing program costs, and
- who is benefiting from the program.

We conducted our audit work from June 1984 through December 1985 at HUD headquarters in Washington, D.C., and at its field offices in Boston, Mass.; Chicago, Ill.; Denver, Colo.; Fort Worth, Tex.; Greensboro, N.C.; Los Angeles, Calif.; Jacksonville, Fla.; Pittsburgh, Pa.; Philadelphia, Pa.; and San Francisco, Calif. To provide a national perspective on the program, we selected these offices on the basis of the number of units funded in fiscal years 1982 and 1983—35 and 37 percent of total units, respectively—and their geographic location. At each office, we interviewed HUD officials. We also visited 49 projects where we interviewed project sponsors and/or managers to obtain information on the issues discussed in this report. We also obtained and reviewed applicable legislation and HUD regulations, policies, and procedures relevant to the review issues.

To determine whether cost containment was working at each of the HUD offices visited, we reviewed HUD records for selected projects constructed before and after cost containment requirements were implemented in November 1981. For those projects constructed under HUD's cost containment requirements, we selected projects that either had completed construction or had a firm commitment for funding from HUD. We did not select any projects that had not reached firm commitment because the sponsor and HUD had not reached final agreement on project characteristics and costs. In total, we selected 85 cost containment projects.

We also selected 94 projects that were not funded under cost containment. In selecting these projects, we first looked at those approved by HUD for funding in fiscal year 1981. Because many of these projects did not have a firm commitment before HUD implemented cost containment, these projects had to comply with some, but not all, of the cost containment requirements. For example, most of these projects rarely had to comply with HUD's requirement regarding the minimum number of efficiency units. We excluded these hybrid projects and others like them from our analyses. However, if HUD records showed that the project was not subject to any cost containment requirements, we considered the project a precost containment project. Working backwards in time, we used the same general procedures to select projects funded in 1980 and 1979, until we had about the same number of precost containment projects as the number of cost containment projects selected. The precost containment projects we selected had either completed construction or were under construction at the time of our review. We did not select any project which started construction before January 1, 1980.

In analyzing the costs of projects built before and after cost containment, we compared similar projects. That is, we analyzed and compared low-rise projects without elevators, two- to four-story projects with elevators, and high-rise projects (five or more stories) with elevators. We adjusted the cost data to 1984 dollars using the Boeckh construction index for the United States.[2]

In addition to our analysis of section 202 projects at the 10 HUD area offices, we also evaluated the impact of cost containment by obtaining and analyzing project data from 2 HUD computerized data bases—the Multifamily Insured and Direct Loan Information System and the Computerized Underwriting Processing System as of January 1985. The first data base provides a chronology of project development from the original application through final construction and operation. The second data base provides construction cost data. By matching the project name and address, we merged information from the two data bases for 802 section 202 projects and determined which projects were built under precost and post-cost containment provisions. We then made cost comparisons of the projects.

We did not analyze samples of the two data bases to verify their accuracy. However, in instances where we found obviously incorrect data, we corrected the cost data based on other supporting HUD documents. In addition, we compared the results of our computerized analysis of project costs with our manual analysis at the 10 HUD area offices. We found the data from both analyses showed a similar impact of cost containment on project costs.

Our assessment of possible further cost reductions in the program was based on our review of project data and HUD's policies and procedures and on discussions with HUD officials, project sponsors, or their management agents. We also analyzed cost data for projects with different structural types and different unit mixes (i.e., efficiencies and one-bedroom units).

[2]This is a generally accepted index in the construction industry used for measuring changes in construction costs.

To determine who is benefiting from the program, we randomly sampled 150 of the 1,262 section 202 projects that had elderly tenants and were constructed after 1974. We took the sample from HUD's Multifamily Insured and Direct Loan Information System. We then requested the respective HUD field offices to provide us with the most recent section 8 tenant income certification forms. Overall, we received 11,609 tenant income certification forms for 142 projects. Data from the remaining eight projects showed that these projects were largely serving the handicapped, so we did not include them in our sample. As agreed with the requester, our review focused primarily on projects serving the elderly.

In addition, we analyzed data from the 1981 Annual Housing Survey to determine the extent to which elderly-headed households had a need for physically adequate and/or more affordable housing. We used 1981 survey data because the data elements we considered in determining need were not yet available from subsequent surveys. We used the housing needs data to evaluate HUD's allocation and use of section 202 loan funds.

Except as noted above, we made our review in accordance with generally accepted government auditing standards.

# HUD's Cost Containment Requirements Reduced Project Costs but Should Be Applied More Consistently

Under HUD's cost containment initiatives, section 202 housing is more modest than housing built before cost containment. Projects built under cost containment had smaller units and fewer amenities. This resulted in reductions in project costs, rents, and associated federal rental subsidies. Without these reductions, we estimate that HUD would have needed about $100 million more to fund the 12,400 units approved in fiscal year 1985.

HUD's cost containment requirements, however, were not applied to all projects. As a result, costs were not reduced as much as they could have been if all projects had been subject to cost containment. The requirements were not applied because as authorized in HUD's instructions, field offices excluded projects with rents of 100 percent or less of FMRS from HUD's supplemental cost containment guidelines. Some of these exempted projects had features that otherwise would have been precluded by HUD guidelines. Cost reductions were also lost through some field offices' use of waivers to HUD's requirement that 25 percent of a project be comprised of efficiencies. Although waivers are allowed when efficiencies are not marketable, HUD should reexamine this policy because of the (1) large single elderly population in need of housing assistance, (2) success in marketing efficiencies to the single elderly in some areas, and (3) cost reductions foregone as a result of providing waivers.

HUD requires only projects with rents in excess of 110 percent of FMRS to undergo a review by headquarters for compliance with cost containment. This resulted in projects at only half of the HUD field offices we visited being subject to headquarters' compliance reviews. Since projects from half of HUD's field offices were not subject to these reviews, HUD's ability to monitor whether its cost containment guidelines are being effectively and consistently applied is lessened.

## Projects Costs and Rents Were Reduced Under Cost Containment

Nationwide, section 202 projects costs were reduced by about 16 percent under cost containment. At the 10 offices we visited, section 202 loan amounts were reduced an average of 14 percent, which had the effect of reducing project rents an average of about 10 percent.

## Cost Containment Requirements

HUD's cost containment requirements, issued in November 1981 (see table 2.1), imposed specific limits on the type and size of units, amenities, and commercial space that could be included in a project. All projects were expected to meet these basic requirements to be eligible for program assistance.

**Table 2.1: Cost Containment Provisions for the Section 202 Elderly Housing Program**

| Requirement categories | Description |
|---|---|
| Unit size | Limited to 415 square feet for efficiencies, 540 square feet for one-bedroom units, and 800 square feet for two-bedroom units. |
| Efficiency units | 25 percent of the units in each elderly housing project must be efficiencies, unless efficiencies are not "readily marketable." |
| Cost not attributable | The total cost of nondwelling space normally should not exceed 10 percent of total project cost, and common rooms must be designed to serve multipurpose functions. |
| Two-bedroom units | Prohibited for the nonhandicapped elderly except for the resident manager's unit. |
| Commercial space | Limited to 5 percent of total project square footage, and proposed commercial activities must be self-supporting and of direct service to tenants. |
| Amenities and design | Amenities and design features are to be controlled to reduce development costs. |

In addition to these basic requirements, HUD issued supplemental guidelines (see app. II) in May 1983 to help HUD field offices and project sponsors eliminate costly features. These features include ceiling heights of over 8 feet, elaborate signs, underground parking, and elaborate entrances.

## Cost Containment Lowered Project Costs and Rents

Our analysis of cost data contained in HUD's Computerized Underwriting Processing System for 802 section 202 projects approved or constructed on or after January 1, 1980, showed that development costs, excluding land and certain fees, for cost containment units averaged 16 percent (inflation adjusted) less than those for precost containment units.

At the 10 field offices we visited, development costs and section 202 loans for units at the 85 cost containment projects reviewed averaged about 14 percent (inflation adjusted) less than the development costs and loans for units at the 94 precost containment projects reviewed. Because of these savings, rents were reduced an average of 10 percent, which directly benefited the government by lowering the section 8 rent subsidies for tenants in these projects. Table 2.2 shows reductions in loan amounts and our estimate of the effect of this on project rents for projects we reviewed at the 10 HUD offices.

**Table 2.2: Loan and Rent Reductions Per Unit Under Cost Containment**

Reductions in Percent

| Field office | Loan reduction (inflation adjusted) | Estimated rent reduction |
|---|---|---|
| Pittsburgh | 25 | 18 |
| Boston | 17 | 12 |
| San Francisco | 16 | 12 |
| Los Angeles | 16 | 12 |
| Jacksonville | 13 | 9 |
| Fort Worth | 13 | 8 |
| Denver | 12 | 8 |
| Philadelphia | 10 | 7 |
| Greensboro | 9 | 7 |
| Chicago | 9 | 6 |
| **Average** | **14** | **10** |

For fiscal year 1985, HUD received $600 million in section 202 loan authority to fund 12,400 units. We estimate that without the 14- to 16-percent cost reduction from cost containment, HUD would have needed an additional $98-$114 million to fund these units.

## Changes in Project Characteristics

A comparison of precost and post-cost containment projects showed that project characteristics changed substantially. Projects constructed under cost containment averaged 11 percent less space, more efficiencies, and fewer amenities. Table 2.3 shows characteristics of precost and post-cost containment projects at the national level and at the 10 field offices visited. Photographs of precost and post-cost containment projects in Clearwater, Florida, and Los Angeles, California (figs. 2.1-2.4) illustrate some of these changes.

**Table 2.3: Comparison of Project Characteristics Between Precost and Post-Cost Containment Projects**

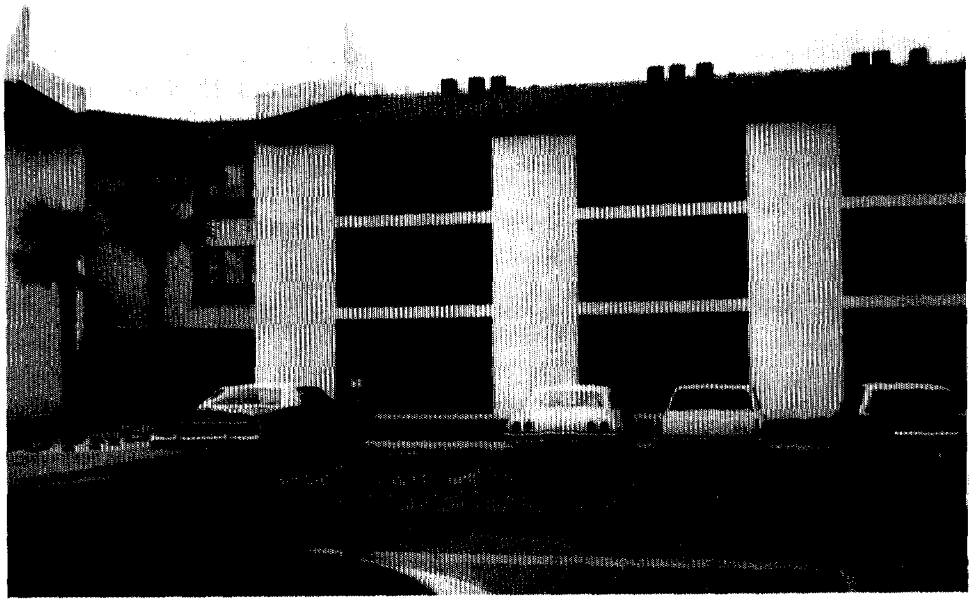
| | Nationwide[a] | | | Projects included in GAO review | | |
|---|---|---|---|---|---|---|
| Characteristic | Pre- | Post | Percent change | Pre- | Post | Percent change |
| Average gross square foot per unit[b] | 814.0 | 720.0 | −11.5 | 818.6 | 732.0 | −10.5 |
| Average square foot per unit | 563.0 | 507.0 | −9.9 | 555.0 | 502.0 | −9.5 |
| One-bedroom size (square foot) | 563.0 | 529.0 | −6.0 | 555.0 | 528.0 | −4.9 |
| Percentage of projects without efficiencies | 88.3 | 34.2 | −61.3 | 92.6 | 17.6 | −81.0 |
| Percentage of units that were efficiencies | 3.0 | 19.7 | +556.7 | 1.8 | 23.6 | +1211.1 |
| Percentage of cost not attributable to dwelling space | 8.0 | 6.0 | −25.0 | 9.6 | 6.7 | −30.2 |
| Percentage of projects exceeding 5 percent for commercial space | 1.9 | 0.0 | ([c]) | 4.3 | 0.0 | ([c]) |
| Percentage of units which were two-bedroom units | 2.5 | .2 | −92.0 | 1.7 | .1 | −94.1 |

[a]Projects included in HUD's Computerized Underwriting Processing Systems.

[b]Includes a pro-rata share of common space.

[c]Not computable.

**Figure 2.1: Precost Containment Project in Clearwater, Florida**

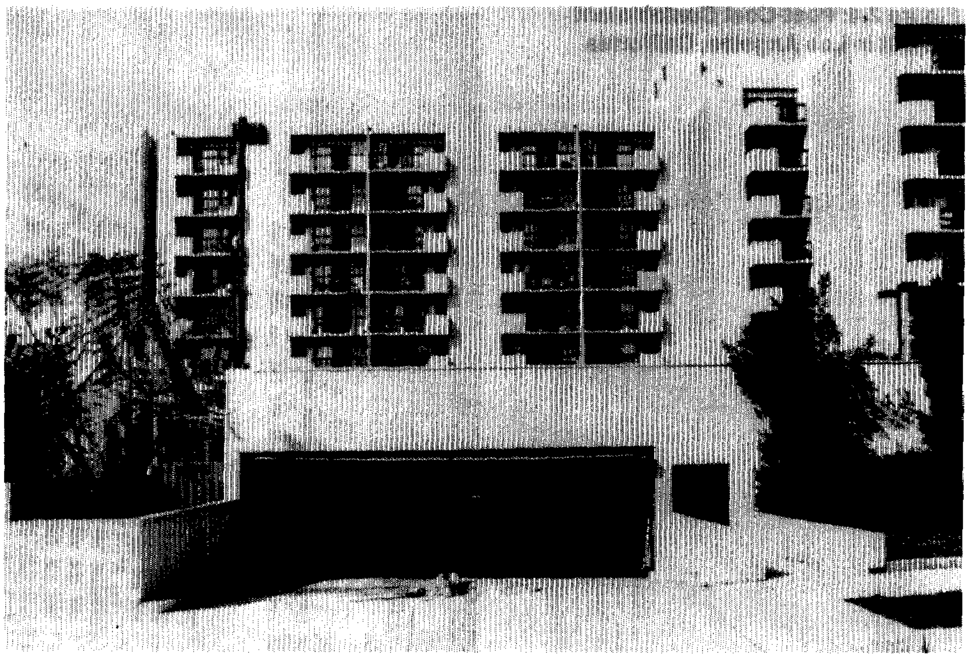


The precost containment project consisted of 100 one-bedroom units (585 sq. ft. each) with balconies and kitchen/dining rooms. The building had a hobby shop and library reception room. The cost not attributable to dwelling use was 14 percent of the section 202 loan amount. Project cost per unit was $51,900 (in 1984 dollars).

**Figure 2.2: Post-Cost Containment Project in Clearwater, Florida**

The post-cost containment project consisted of 21 efficiencies and 61 one-bedroom units. Each one-bedroom unit contained 540 square feet. Because of cost-containment restrictions, HUD had the sponsor remove the irrigation system, covered walk, and waste compactors, among other items. The cost not attributable to dwelling use was 3 percent of the section 202 loan amount. Project cost per unit was $41,540 (in 1984 dollars).

**Figure 2.3: Precost Containment Project in Los Angeles, California**



The precost containment project consisted of 150 one-bedroom units (averaging 562 sq. ft. each) with balconies. The project had an underground garage. The balconies cost $168,300, and the underground garage cost $195,000. Cost not attributable to dwelling use was 7 percent of the section 202 loan amount. Project cost per unit was $91,800 (in 1984 dollars).

**Figure 2.4: Post-Cost Containment Project in Los Angeles, California**

The post-cost containment project consisted of 150 one-bedroom units and 50 efficiency units. The one bedroom units measured an average of 518 square feet, and the efficiences measured 413 square feet each. Following cost containment guidelines, the project had an outside parking lot, which cost $34,000. Cost not attributable to dwelling use was 4 percent of the section 202 loan amount. Cost per unit was $58,780 (in 1984 dollars).

HUD's unit size limits and efficiency and amenity requirements had the most noticeable impact on projects. At 8 of the 10 field offices visited, the precost containment projects reviewed had one-bedroom units that, on the average, exceeded the 540-square-foot limit imposed by cost containment. Projects at two of the HUD offices reviewed (Fort Worth and Greensboro) had the largest one-bedroom units—578 square feet and 585 square feet, respectively. In contrast, the cost containment projects reviewed at 9 of the 10 HUD offices had one-bedroom units that averaged 540 square feet or less. At the remaining HUD office, they averaged 542 square feet.

HUD's requirement that 25 percent of a project's units be efficiencies substantially increased the number of such units in cost containment projects. Before cost containment, only 2 percent of the units in the projects we reviewed at the 10 offices were efficiencies, compared with 24 percent under cost containment. Together with the 415-square-foot limit for these units, HUD's efficiency requirement had the effect of limiting the average rental size of all units to 509 square feet (25 percent efficiencies x 415 square feet + 75 percent one-bedroom units x 540 square feet). Before cost containment, the average size of units for the projects we reviewed exceeded 509 square feet at all 10 of the field offices. In contrast, projects constructed after cost containment at 8 of the 10 offices visited had an average unit size of 509 square feet or less. Projects at the remaining two HUD offices (Boston and Greensboro) did not meet the average square footage limit in part because these offices waived HUD's efficiency requirement. (See p. 27.)

Cost containment prohibited projects from having the following amenities: balconies, atriums, trash compactors, and dishwashers. Besides prohibiting certain amenities, cost containment generally placed a 10-percent limit on "cost not attributable to dwelling use" which includes such items as community rooms and parking space. Thirty-nine (41%) of the 94 precost containment projects reviewed exceeded this limit. In contrast, only 4 of the 85 cost containment projects reviewed exceeded this limit.

HUD's prohibition against two-bedroom units virtually eliminated these units at the cost containment projects we reviewed. Similarly, none of the cost containment projects reviewed exceeded HUD's 5-percent limit on commercial space. These requirements, however, had less of an overall impact because few precost containment projects had exceeded these limits. Of the precost containment projects reviewed, only 2 percent of the units were two-bedroom units and only 4 percent had commercial space exceeding 5 percent.

## Inconsistencies in the Application of Cost Containment

HUD's supplemental cost containment guidelines were not applied to all projects because HUD field offices exercised discretion provided by HUD instructions to exempt projects with rents of 100 percent or less of FMRs from compliance with these guidelines. Some of these exempted projects, however, had features that otherwise would have been precluded had these guidelines been applied to all projects. As a result, HUD could have realized greater cost reductions if cost containment had been applied in all cases.

Costs were also not reduced as much as possible because HUD allowed field offices to waive HUD's 25-percent efficiency requirement when these units were not considered marketable. Efficiencies, however, have been successfully marketed to the single elderly in some areas. Furthermore, they are less costly to construct than one-bedroom units, and HUD considers them the most appropriate way to house the single elderly.

Also, projects at only half the HUD field offices we visited were subject to HUD reviews to determine compliance with cost containment. This happened because HUD required only projects with rents in excess of 110 percent of FMRs to undergo compliance reviews. Because headquarters compliance reviews covered projects from only some HUD offices, HUD has less assurance that cost containment was applied effectively and consistently by all its offices.

## Exemptions From HUD's Supplemental Cost Containment Guidelines

In issuing its supplemental cost containment guidelines, HUD instructed its field offices that it would not object if one or more of the features precluded by these guidelines were included in a project as long as project rents were 100 percent or less of FMRs. Of 85 cost containment projects we reviewed, 22 had rents of 100 percent or less of FMRs, making these projects eligible for exemption from HUD's guidelines. While we did not attempt to determine whether all these projects had features that otherwise would have been precluded by HUD's guidelines, we noted that some did. For example, at HUD's Boston office, one three-story project had three elevators. All other elevator projects we reviewed had only one or two elevators. Because this project had rents of less than 100 percent of FMRs, the regional office did not require it to comply with HUD's guidelines, which called for minimizing the number of elevators included in projects. This increased the project's construction costs. At another project, in HUD's San Francisco office, HUD records showed that although the project had several costly features—such as unusual roof and building configurations—that were contrary to HUD's guidelines, no changes were required because project rents were 100 percent or less of FMRs.

According to headquarters officials, HUD never intended to exempt projects from these guidelines. However, the officials agreed that HUD's instructions give this impression. According to the director of HUD's Technical Support Division, HUD is now in the process of drafting instructions to clarify that these guidelines should be applied to all projects regardless of the relationship of project rents to FMRs.

## Extent and Rationale for Efficiency Waivers

Under cost containment, HUD requires that 25 percent of a project be comprised of efficiency units. As part of its cost containment requirements, however, HUD gave its field offices the authority to waive this requirement on a project-by-project basis when efficiency units were not readily marketable. Nationwide, 34 percent of the cost containment projects had no efficiencies. (See table 2.3.) At the 10 HUD offices we visited, 15 (18 percent) of the 85 cost containment projects reviewed had no efficiencies because of waivers granted by HUD field offices. These projects were located in HUD's Boston, Denver, and Greensboro offices.

**Table 2.4: Percentage of Projects Receiving Efficiency Waivers**

| Location | Projects reviewed | Projects with efficiency waivers: Number | Percent |
|---|---|---|---|
| Greensboro | 12 | 9 | 75 |
| Denver | 7 | 4 | 57 |
| Boston | 9 | 2 | 22 |
| **Total** | **28** | **15** | **54** |

HUD's Boston office granted waivers on two projects for reasons other than marketability. Contrary to HUD's requirements, one project was granted a waiver because proposed rents were less than 100 percent of the area's FMRS. This field office did not believe cost containment applied to such projects. The other project was granted a waiver with headquarters' approval in exchange for agreeing to obtain competitive bids for project construction. HUD's Greensboro and Denver offices, which granted the largest number of waivers, did so because the units were not considered marketable.

### Greensboro

Until March 1983, HUD's Greensboro office had a policy of waiving the efficiency requirement for all projects in North Carolina because it questioned whether these units were marketable. In support of this position, HUD officials cited statistics showing that efficiencies (1) accounted for less than 1 percent of the housing stock in the state and (2) had a higher vacancy rate than larger rental units. After March 1983, the Greensboro office changed its policy to grant waivers on a case-by-case basis. Although six of the projects we reviewed were subject to this new policy, only two had efficiencies.

We asked HUD Greensboro officials why they were not complying with HUD's policy of requiring that 25 percent of a project's units be efficiencies. In response, they questioned whether efficiency units are marketable in their state. As evidence of this, one field office official cited a public housing project located in Greensboro with efficiency units that had considerable difficulty in renting them. However, upon visiting this project, public housing officials informed us that they were having little difficulty in renting these efficiencies. While HUD's Greensboro officials questioned the marketability of efficiencies, they agreed that these units could be rented when no one-bedroom, subsidized units were available.

### Denver

Waivers were granted on four of the seven projects we reviewed at this office, in part because the field office initially questioned the marketability of efficiency units. However, the office's Director of Housing Development told us that a more significant issue was the cash flow problem that efficiencies created for project sponsors. As discussed in chapter 3, the FMRS for efficiency units can create cash flow problems that could jeopardize project feasibility. In the case of HUD's Denver office, however, these cash flow problems could have been reduced if the Denver office had not established a policy of limiting project rents to 110 percent of FMRS. In this way, projects with efficiency units could have sought higher project rents—up to 120 percent of FMRS—to reduce or eliminate the cash flow problems created by these units. Regarding the marketability of efficiencies, the director pointed out that subsidized projects in the Denver area have waiting lists for efficiencies.

As discussed in chapter 3, efficiencies have been marketed in some areas where the single elderly need housing assistance. HUD also considers efficiencies an appropriate means for housing the single elderly. Because they cost less to build than one-bedroom units (see p. 37, efficiencies also are a more economical means of providing housing assistance to the single elderly. In addition, as discussed in chapter 4, 2.5 million (61%) of the 4.1 million very low-income elderly who need housing assistance are single. Accordingly, a finding that efficiencies are not marketable should, in our opinion, cause HUD to reassess whether it should finance such projects.

Besides allowing waivers, HUD does not require projects with waivers to meet the smaller space and lower rent constraints (FMRS) that are applicable to projects with efficiencies. Projects with 25 percent of their space comprised of efficiencies cannot have an average unit size exceeding 509 square feet. (See p. 25.) The projects granted waivers that we reviewed, however, had units that averaged 527 square feet. Projects with efficiencies are required by HUD to use the FMRs for efficiencies, which are lower than the FMRs for one-bedroom units. However, projects that obtain waivers and therefore build more one-bedroom units can use the higher FMRs for one-bedroom units. The use of these higher FMRs, together with the larger size units in projects with waivers, lowered the reductions that could have been realized from cost containment.

## HUD Needs to Extend Compliance Reviews to All Offices

In issuing its supplemental cost containment guidelines, HUD informed its field offices that projects with rents exceeding 110 percent of the FMRS would be subject to a headquarters review for compliance with cost containment. According to the section 202 program director, HUD elected to use this limit because projects were already subject to headquarters approval when their rents exceeded 110 percent of FMRS.

Of the 85 cost containment projects we reviewed, 63 (74%) had rents of 110 percent or less of FMRS, thereby exempting them from a headquarters compliance review. Twenty-two of these projects were located in HUD's Denver, Fort Worth, and San Francisco offices. These three offices had established a policy of limiting rents to 110 percent of FMRS. None of the 30 projects we reviewed in HUD's Boston, Jacksonville, or Los Angeles offices had rents exceeding 110 percent of the FMRS. In all, projects at 6 of the 10 HUD offices we visited were not subject to headquarters compliance reviews based on the 110-percent FMR criteria.[1] In contrast, all 12 projects reviewed at HUD's Chicago and Pittsburgh offices were subject to headquarters compliance reviews.

Because a representative sample of projects from each HUD office was not subject to a headquarters compliance review, HUD's ability to monitor cost containment at all its offices was lessened. For example, a HUD official at the Denver office stated that the office did not fully apply HUD's supplemental guidelines, contrary to HUD's requirements, to projects with rents of 110 percent or less of FMRS. Because Denver allows no projects to have rents of more than 110 percent of FMRS, the field office's projects are not subject to compliance review. This lessens HUD's ability to know whether the field office is applying the supplemental guidelines.

[1]One of the Denver office projects had rents in excess of 110 percent of FMRs, but this was an exception to that office's policy of restricting rents to 110 percent of FMRs.

Considering that HUD's supplemental guidelines are by necessity somewhat vague, compliance reviews are essential for ensuring reasonable consistency in how HUD field offices apply cost containment guidelines. For example, HUD's guidelines require project landscaping to be minimized. Landscaping needs to be tailored to each project, making it difficult, if not impossible, to develop specific standards. In this respect, we noted that one HUD office precluded the use of underground sprinkler systems at all its projects, while another office did not. Because neither office was required to submit its projects for compliance reviews, headquarters was not in a position to determine whether inconsistencies such as this were appropriate. Aside from ensuring reasonable consistency, compliance reviews have resulted in additional cost savings. This is because when HUD finds instances of noncompliance, it generally requires sponsors to delete or pay for any costly features.

## Conclusions

HUD's cost containment initiatives have resulted in about a 14- to 16-percent savings in project construction cost. HUD's supplemental requirements, however, were not applied consistently to all projects because some HUD field offices exercised their discretion to exempt projects with rents of 100 percent of FMRs or less from these guidelines. Consequently, some of these projects contained features that were precluded by HUD's guidelines. Applying HUD's supplemental guidelines to all projects would better ensure consistency while providing opportunities for greater cost reductions. HUD agrees and clarified its instructions to accomplish this.

HUD's policy of allowing field offices to waive its efficiency requirement also lessened the reductions realized from cost containment. In light of the (1) large single elderly population in need of housing assistance, (2) success in marketing efficiencies to the single elderly in some areas, and (3) cost reductions foregone as a result of providing waivers, HUD needs to reexamine this policy.

Under HUD's current policy, compliance reviews were made on projects at only half of the HUD offices we visited. This occurred because HUD only subjected projects with rents exceeding 110 percent of FMRs to these reviews. Projects at half of the offices reviewed, however, had rents of 110 percent or less of FMRs, thereby lessening HUD's ability to ensure its requirements were applied effectively and consistently by each of its offices. If HUD had subjected a sample of projects from each of the offices to compliance reviews, HUD would have been in a better position to monitor field office compliance with cost containment.

## Agency Comments and Our Evaluation

In commenting on our draft report (see app. V), HUD stated that it had instructed its field offices on April 2, 1986, to apply cost containment and modest design requirements to all projects regardless of the relationship of project rents to FMRS. Field offices also were instructed to objectively examine every project proposal to ensure cost-efficient design, and were provided with more specific guidance to assist in project design analysis. HUD also stated that its field offices will receive training on the new instructions during June 1986. If properly implemented, these actions should ensure greater consistency in the application of cost containment.

Concerning compliance reviews, HUD stated that it is currently addressing this matter through headquarters' ongoing monitoring of field offices. Specifically, HUD stated that it had conducted to date in fiscal year 1986 on-site field office reviews in Minneapolis, New Orleans, Newark, Pittsburgh, Los Angeles, and San Francisco, with specific emphasis on reviewing section 202 projects in the design stage for compliance with cost containment objectives. HUD stated that these on-site reviews are superior to a headquarters compliance review of selected exhibits because at the site, the entire processing file is available for review. Furthermore, field office staff can be questioned on different matters. In addition, HUD stated that training can be conducted on the spot when deficiencies are discovered.

In view of the importance HUD places on field site reviews, we discussed HUD's comments with the Director of HUD's Technical Support Division, which is responsible for monitoring field office compliance with cost containment. According to the Director, she has the resources (staff and travel funds) to do about 10 on-site reviews annually. In contrast, the Director stated that several years ago, she had sufficient resources to do on-site reviews of each office biennially. The Director also stated that she did not have the resources to do compliance reviews on additional projects to ensure coverage of all its offices while simultaneously conducting both on-site reviews and compliance reviews of projects requiring the Secretary's approval of project rents (those exceeding 110 percent of FMRS). According to the Director, the latter could not be discontinued because this was a program requirement.

While we agree that on-site reviews provide a more in-depth analysis on cost containment's implementation, this coverage is limited. With about 50 field offices, each is subject to on-site review about once every 5 years. Further, headquarters' compliance reviews are limited only to those projects with rents over 110 percent of FMRS. As we pointed out in this chapter, only about half of the offices visited had projects subject to these compliance reviews. As a result, HUD does not have assurance that all its field offices have properly applied cost containment.

HUD also stated that it wanted to retain its policy of allowing waivers to its requirement for efficiency units because serious resistance to efficiency units could occur in some circumstances. HUD stated that the subsidization of section 202 projects by section 8 rental assistance does not guarantee that all units will be easily marketed. As evidence for this position, HUD stated it was beginning to see serious problems in renting units in different parts of the country. HUD recognized that the waiver provision could be strengthened, and stated that it will rescind field office authority to grant waivers when implementing its fiscal year 1987 program. Instead, HUD will grant them only at headquarters.

## Recommendations to the Secretary of Housing and Urban Development

To provide greater consistency in the application of cost containment, we recommend that the Secretary of HUD should select a sample of projects for compliance review from each of its field offices. In addition, we recommend that the Secretary reexamine whether HUD's policy of allowing waivers to its efficiency requirement should be continued.

# Alternatives for Making the Section 202 Program More Cost-Effective

Through its cost containment efforts, HUD has reduced section 202 program costs. Program costs, however, could be further reduced if

- efficiency units were used more to house the single elderly and
- HUD's project selection process gave greater consideration to the project's modest design.

## Greater Use of Efficiencies Would Further Reduce Program Costs

Occupancy criteria for HUD's subsidized housing programs indicate that efficiencies are adequate units for single individuals. Efficiencies are also less costly to construct than one-bedroom units. Over 80 percent of the elderly tenants living or moving into section 202 projects are single. Despite this, most single elderly tenants continue to be housed in more expensive one-bedroom units.

Two factors influence the number of efficiencies included in any one project—and thus the number of single elderly living in them. First, HUD is precluded by law from requiring projects to have more than 25 percent of their space occupied by efficiencies. Second, sponsors lack financial incentives to include efficiencies in their projects. However, we estimate that program construction costs could have been reduced by $19 million in fiscal year 1985, if 80 percent of the units built were efficiencies. Although the single elderly who otherwise would have been housed in one-bedroom units would receive smaller units, the resulting cost reductions could be used to help house more of the 4 million elderly headed households in need of housing assistance.

## Efficiencies Are Only Used to a Limited Extent to House the Single Elderly

Most of the tenants served by the section 202/8 program are single, and most were single when they moved in. Our sample of almost 12,000 tenants in 142 section 202 projects showed that 87 percent of the tenants were single. At the vast majority of projects sampled (see table 3.1), more than 70 percent of the tenants were single. In addition, 80 percent of the tenants who moved into the sampled projects during 1983-84 were single when they moved in.

**Table 3.1: Distribution of Projects by Percentage of Single Tenants**

| Percentage of single tenants | Projects Number | Percent |
|---|---|---|
| 0 - 49 | 2 | 1 |
| 50 - 69 | 2 | 1 |
| 70 - 79 | 15 | 11 |
| 80 or more | 123 | 87 |
| **Total** | **142** | **100** |

According to HUD occupancy criteria, efficiency units are an adequate means to house single tenants. But for couples or two related adults of the same sex, such as sisters, HUD's criteria indicate that one-bedroom units are more appropriate.

While efficiencies provide the optimal means for housing the single elderly, only 5 percent of the units at the 142 projects we sampled were efficiencies. Most of the units (88 percent) were one-bedroom units. Consequently, most single elderly tenants were housed in one-bedroom units because they constituted 87 percent of all projects' tenants.

As stated earlier, HUD requires that 25 percent of a project be comprised of efficiencies. But even at this level, most single elderly tenants would still have to be housed in one-bedroom units. For example, with a 75/25 percent mix of one-bedroom and efficiency units and a single elderly tenant population of 80 percent, about 70 percent of the single tenants would be housed in one-bedroom units, whereas the remaining 30 percent would be housed in efficiency units.

Regardless of whether a single elderly person occupies a one-bedroom unit or an efficiency, he or she pays the same rent. This is because by law, tenants are required to pay 30 percent of their adjusted income toward rent for any unit they occupy. In the case of single elderly tenants, the size of the unit they occupy may be considerably different. According to our analysis of HUD data for cost containment projects, efficiencies and one-bedroom units averaged 411 and 529 square feet, respectively—a difference of 118 square feet (or a room about 10 feet by 12 feet).

HUD is precluded by section 202 (i)(1) of the Housing Act of 1959, as amended by the Housing and Urban-Rural Recovery Act of 1983, from requiring projects to have more than 25 percent of their space comprised of efficiencies. The legislative history is unclear as to why the Congress believed section 202/8 projects should not be required to have more than 25 percent of their units comprised of efficiencies. According to HUD officials, the 25-percent limit represented a compromise between section 202 sponsors who did not want any efficiencies and those who felt that more use of efficiencies would result in a larger number of the needy elderly being housed.

A few sponsors have voluntarily included more efficiency units in their projects than the number required by HUD. Of the 85 cost containment projects we reviewed, 10 had 30 percent or more of their space occupied by efficiency units, and 3 of them had 50 percent or more of their space occupied by efficiencies.

## More Efficiency Units Could Be Built by Adjusting FMRs for These Units

According to several HUD officials, sponsors have been reluctant to construct more efficiencies in their projects than those required by HUD because FMRs for these units can have an adverse effect on the project's financial feasibility. Such an effect can occur because private sector rents for efficiency units on which FMRs are based do not cover average total costs. FMRs are set by selecting a sample of rents from an area's market of private rental units. Efficiency units account for about 1 percent of the rental housing stock. For the most part, they are included in private rental projects to utilize space that otherwise would not be used. Thus, the variable costs of constructing efficiencies is a smaller part of total costs than for other units. This allows landlords to reduce the rent on efficiencies without necessarily losing money.

FMRs that do not cover average total costs would be expected to have a negligible effect on the project's financial feasibility when only a few efficiency units are involved. However, as the percentage of efficiencies increases, the lower rents reflected in efficiency FMRs could eventually reduce project revenues to the point where revenues are no longer sufficient to cover the construction and operating costs required for a viable project.

We observed the adverse effect of FMRs for efficiencies on a project's financial feasibility at HUD's Philadelphia office. On this project, the sponsors had proposed to construct a project with over 80 percent of its space occupied by efficiency units—53 efficiency units and 12 one-bedroom units. However, the rent revenues provided by FMRs were insufficient to support project construction and operating costs. According to the project architect, the sponsor initially changed the project design by reducing the size of efficiencies to 393 square feet. Even with these changes, the sponsor found that project revenues provided by FMRs were insufficient to support the project. To make the project financially feasible, the sponsor converted 12 of the efficiency units into one-bedroom units, thereby getting the benefit of these units' higher FMRs.

Although the FMRs for efficiency units can provide a disincentive for building efficiencies, HUD could resolve this problem by adjusting the rents for efficiency units to more accurately reflect the construction and operating costs associated with building them. For example, at five of the HUD offices we visited, HUD officials estimated that efficiencies cost from about $1,500 to $5,100 less per unit to construct than one-bedroom units. (See table 3.2.) On the basis of these cost differences, we estimated that the rents for efficiency units should be $13 to $44 less than the rents for one-bedroom units.

At the five offices, differences were much larger than our estimates. For example, at projects we reviewed in HUD's Chicago office, efficiencies provided $124-$134 less in monthly rents than did the FMRs for one-bedroom units on the basis of FMRs. With $134 less in rents, we estimate that project construction costs would have to be reduced by $15,600 for each efficiency included in the project, even though an efficiency there was estimated by HUD to cost only $2,600 less than the cost of a one-bedroom unit. In contrast, if the FMRs for efficiency units were only $22 less than the FMRs for one-bedroom units, we estimate that project costs would have to be reduced by only $2,600 for each efficiency included in the project.

**Table 3.2: Estimated Construction Cost Difference Between an Efficiency Unit and a One-Bedroom Unit**

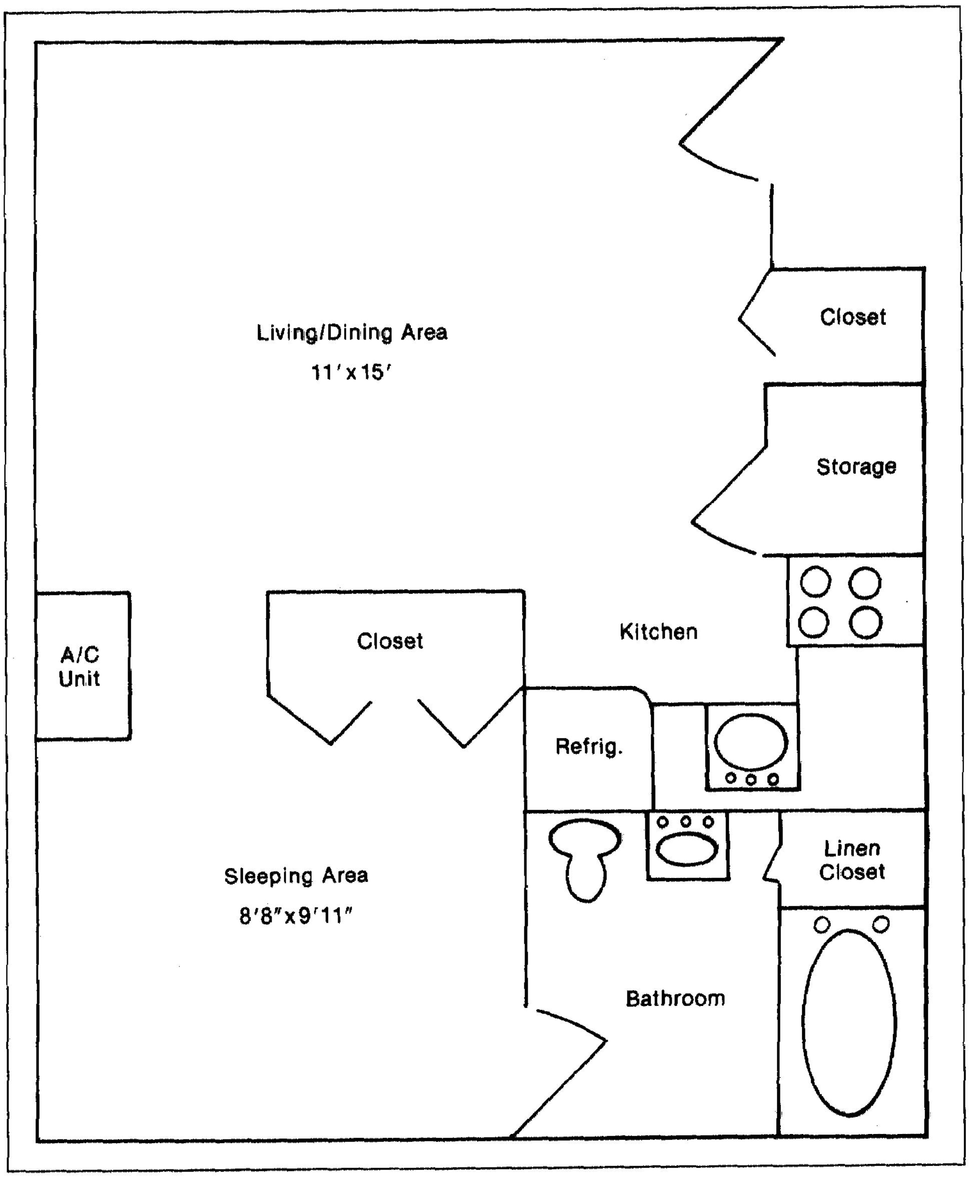
| HUD area office | Estimated cost difference |
|---|---|
| Pittsburgh | $1,500 |
| Los Angeles | $2,200 |
| Denver | $2,600 |
| Chicago | $2,600 |
| Jacksonville | $5,100 |

## Other Concerns About Efficiency Units Can Be Overcome

Besides the disincentives FMRs can create in building efficiencies, we asked sponsors and HUD field staff whether they had other concerns regarding efficiencies. Their reactions were mixed. One major concern frequently voiced by sponsors was that because efficiency units were small and lacked privacy, they were less desirable than one-bedroom units. They stated that elderly individuals have difficulty adjusting to life in a single room, particularly one in which the living area and bedroom space are combined, after having lived in a multi-room dwelling. They added that these individuals must divest themselves of treasured possessions because of the limited living space in efficiency units. Sponsors characterized the process as "transition shock." Concerning privacy, sponsors stated that tenants dislike having their entire unit, including the bedroom area, fully visible to visitors.

These views, however, were not shared by others we contacted. For example, some field office officials and sponsors told us that better-designed efficiency units could enhance their attractiveness (marketability). For example, a national section 202 program sponsor adopted a unit design that incorporated a separator between the living room and the bedroom area. According to the sponsor's representative, the elderly have accepted this design because it provides privacy and is an aesthetically appealing unit. The sponsor is planning to incorporate this design in future projects. Figure 3.1 shows the layout of this unit.

**Figure 3.1 Layout of Efficiency Unit**




Source: National Church Residences.

Other sponsors also were able to successfully market efficiencies where there was a need for housing assistance. According to HUD officials in San Francisco, efficiency units were readily marketable there because of the shortage of housing. A project sponsor in Los Angeles, who was in the process of completing construction on a 200-unit project, told us that he already had more than enough applicants to occupy the project's units, including its efficiency units. This sponsor stated that most of the applicants were paying considerably more for housing than they will pay for these section 202 units, and therefore will be pleased to live in the project's efficiency units. This sponsor, however, did foresee a problem in assigning single applicants to the project's one-bedroom and efficiency units. The sponsor stated that they would probably use a lottery to accomplish this.

Considering the success of these sponsors, we believe efficiencies can often be marketed successfully to single elderly persons. As discussed in chapter 4, over 4 million elderly headed households, consisting largely of single elderly persons, have a need for housing assistance.

Two sponsors also stated that efficiencies increase administrative costs. They said that residents who must live in efficiencies immediately put their names on the waiting list for one-bedroom units in the project. As vacancies occur, these individuals move to the more spacious units. As a result, sponsors said they have to prepare two units for occupancy instead of one—a one-bedroom unit to be reoccupied internally, and a vacated efficiency unit. Other project sponsors, however, resolved this problem by prohibiting such moves.

### Benefits From Increasing the Use of Efficiencies

In fiscal year 1985, HUD funded 12,400 new units in the section 202 program. If 80 percent, rather than 25 percent, of these units had been efficiencies (to match the percentage of the single elderly population moving into section 202 projects), approximately 6,800 more efficiencies rather than one-bedroom units could have been built. On the basis of an average savings of $2,800 for each efficiency, we estimate that this would have reduced construction costs and section 202 loan authority by $19 million—or enough to build about 400 more units.

## Project Construction Costs Should Be Given Greater Consideration in Selecting Projects

HUD could better ensure that it funds the least costly projects by giving greater consideration to project construction costs during project selection. HUD receives far more applications than it can fund. Although project costs vary widely, HUD has directed its field offices not to consider the sponsor's cost estimate in rating and ranking projects for selection. Instead, HUD evaluates the project's land cost and modest design features in making project selections. Although HUD considers modest design features as part of its project selection process, field offices did not use the modest design evaluations to identify the least costly projects. In addition, the rating process used to select projects diminished the importance of the project's modest design, thereby making it possible for more costly projects to be selected for funding.

## Project Costs and Rents Vary Widely

At the 10 HUD field offices we visited, project costs varied widely. At HUD's Los Angeles office, project development costs for cost containment projects differed by as much as 94 percent. At HUD's Fort Worth office, such development costs varied by as much as 84 percent. Additional details are shown in table 3.3.

**Table 3.3: Project Development Costs for Cost Containment Projects Reviewed at Selected HUD Offices**

| | Unit development costs[a] | | |
|---|---|---|---|
| HUD office | Low | High | Difference (percent) |
| Boston | $42,200 | $54,100 | 28 |
| Chicago | 53,000 | 59,200 | 12 |
| Denver | 33,900 | 43,400 | 28 |
| Fort Worth | 24,200 | 44,500 | 84 |
| Greensboro | 27,400 | 35,600 | 30 |
| Jacksonville | 35,900 | 50,900 | 42 |
| Los Angeles | 35,800 | 69,500 | 94 |
| Philadephia | 37,300 | 50,900 | 36 |
| Pittsburgh | 42,500 | 48,700 | 15 |
| San Francisco | 47,300 | 70,900 | 50 |

[a]Development costs, which include land, were inflation-adjusted to 1984 based on the Boeckh construction index.

Rents for these projects also varied widely. The range in FMRs for the various market areas within these HUD offices illustrates this point. For example, for market areas within HUD's Los Angeles office, the FMRs published by HUD in 1985 for one-bedroom units ranged from $410 to $781, a difference of about 90 percent. For market areas within HUD's San Francisco office, FMRs for one-bedroom units varied by as much as 150 percent, from $349 to $873.

These variations in development costs and rents occurred because of differences in such factors as structural type, project design, location (land costs), local building requirements, material and labor cost, and the comparative efficiency with which sponsors and developers completed the projects.

## HUD's Selection Process Could Give Greater Consideration to Project Costs

In selecting projects for funding, HUD allocates funds to each of its field offices. (HUD's allocation formula is discussed in ch. 4.) After receiving their allocations, HUD's field offices solicit applications from interested sponsors. Applications are initially screened for eligibility. HUD then requires each applicant to be rated and ranked on the basis of the selection factors shown in table 3.4. According to HUD instructions, every applicant that meets these selection factors represents an acceptable and approvable project. The rating/ranking process serves only to identify the best projects among those found acceptable. During each of the past 3 fiscal years (1983-85), HUD had three to four times as many acceptable/approvable applications as it could fund.

**Table 3.4: HUD Section 202 Project Selection Process Ranking Factors and Corresponding Point Values**

| Factor | Maximum points |
|---|---|
| 1. The borrower's financial capacity | 30 |
| 2. The borrower's capacity to carry through to long-term operation a project for housing and related facilities | 20 |
| 3. Location (site/neighborhood) | 15 |
| 4. Modest design/cost containment | 25 |
| 5. Special needs (to be rated by the regional office) | 10 |
| **Total** | **100** |

Despite the wide ranges in project costs, HUD has instructed its field offices to disregard the sponsor's cost estimates and not to estimate the project's cost themselves when rating and ranking projects for selection. According to HUD's program director, HUD ignores the sponsor's cost estimate because the sponsor may underestimate costs to improve the chances of being selected. In addition, HUD does not estimate project costs because of concerns over the adequacy of information on project proposals and the delays in the project selection process that preparing estimates would cause.

Although project development costs are not directly considered in making project selections, HUD does attempt to consider these costs when rating the project's location and modest design/cost containment. In evaluating a project's location, HUD field offices can award up to 5 points if the project's site costs per unit are cost effective with respect to the number of units proposed. (The remaining 10 points under this selection factor pertain to the site's acceptability based on criteria other than cost, such as access to public services.)

Under the modest design/cost containment factor, HUD field offices can award projects up to 25 points, to the extent the project complies with the following criteria:

1. Architectural treatment. The overall project design must result in a project that will be economical to construct and efficient to operate. For example, a proposal that included unusual building configurations not required to provide for the needs of the occupants would be looked on unfavorably. Conversely, a project proposal to use construction methods and materials that demonstrably reduce costs would receive favorable consideration. (Maximum of 10 points.)

2. Typical unit design. The proposed floor layouts and unit designs must reflect economical and efficient use of space suitable for the intended occupants. (Maximum of 10 points.)

3. Amenities and special space and accommodations. Items proposed must be necessary and suitable for the intended occupants, and modest in concept. (Maximum of 5 points.)

Although HUD indirectly considers project costs in evaluating the project's modest design, its rating and ranking process allows projects of less modest design to be selected over other more modest projects. This can occur because of the maximum points that can be assigned to other selection factors, particularly the borrower's financial capacity (30 points) and capacity to provide for the long-term operation of the project (20 points). Together, these two factors account for up to half of the points projects can receive. Consequently, projects rated high on these two factors and low on modest design could be ranked higher and selected for funding over a project rated high in modest design but low in financial and/or operational capacity.

A hypothetical situation can illustrate how the project selection process does not necessarily result in the most modestly-designed project being chosen. Assume that project A receives 25 points for both financial and operational capacity and the maximum of 25 points for modest design, or a total of 50 points. On the other hand, assume that project B receives the maximum of 50 points for financial and operational capacity and only 10 points for modest design, or a total of 60 points. In this situation, project B, although of less modest design, would have an advantage over project A in being funded, assuming all other factors were equal.

HUD's rating/ranking process has borne out this example by enabling less modestly designed projects to be selected over more modestly designed projects. For example, in fiscal year 1984, one project in HUD's Los Angeles office received 18 points for modest design and 24 points for financial and operational capacity. Although this project was the second best project in terms of modest design, other less modest projects were selected because of the higher points received for both financial and operational capacity.

While financial and operational capacity are no doubt important factors to consider, the present rating/ranking system hinders the selection of the most modest project. HUD could better assure that the least costly projects were selected by using a two-tiered approach. Under a two-tiered approach, projects would first be rated and ranked on the four factors other than modest design—financial capacity, operational capacity, location, and special needs. Projects found acceptable on the basis of these tier-one factors would then compete for selection in tier two on the basis of modest design/cost containment. The following example illustrates the effect of this two-tiered approach on project selections. The example assumes that all projects received the same number of points for location and special needs.

In fiscal year 1984, 7 projects were selected at HUD's Los Angeles office from among 27 acceptable applications for elderly projects. Each project selected had a combined score of at least 30 points for financial/operational capacity. In all, 17 of the 27 applicants for elderly housing projects had scored 30 points or more on financial/operational capacity. Under a two-tiered approach, all 17 would have been considered acceptable for funding in tier one and placed into tier two to compete on the basis of modest design. These 17 projects would then have been ranked for modest design in tier two. As shown in table 3.5, projects J, L, and N would have been ranked higher and therefore selected before projects C, D, and F, which, although less modest, were selected for funding under HUD's present ranking system.

**Table 3.5: Effect of Two-Tiered Selection System on Projects Selected for Funding**

| Projects selected[a] | Tier one approved projects[b] | Tier two modest design ranking | Change in project selections |
|---|---|---|---|
| A | A | 1st | None |
| B | B | Tied for 2nd | None |
| C | C | Tied for 3rd | Dropped |
| D | D | Tied for 3rd | Dropped |
| E | E | Tied for 2nd | None |
| F | F | 5th | Dropped |
| G | G | Tied for 2nd | None |
| | H | 7th | None |
| | I | Tied for 3rd | None |
| | J | Tied for 2nd | Added |
| | K | Tied for 6th | None |
| | L | Tied for 2nd | Added |
| | M | Tied for 6th | None |
| | N | Tied for 2nd | Added |
| | O | 4th | None |
| | P | Tied for 2nd | None[c] |
| | Q | Tied for 3rd | None |

[a]Projects include only those for the elderly. The minimum number of points any project received for financial/operational capacity was 30.

[b]All elderly projects with 30 points or more for financial/ operational capacity.

[c]We assumed funds would not be sufficient to fund all the projects tied for second.

In ranking projects on the basis of costs in tier two, we would expect HUD to continue its practice of considering a community's housing needs in making final project selections. These needs presently consider a distribution of projects between metropolitan and nonmetropolitan areas, vacancy rates between areas, and communities' prior participation in the program, particularly the funding of projects in localities that have been underfunded relative to their needs.

## Conclusions

Most single elderly tenants in section 202 projects are housed in one-bedroom units. HUD considers less costly efficiency units to be adequate housing for single individuals. By increasing the use of efficiencies to house the single elderly, HUD could have reduced project construction costs by up to $19 million in fiscal year 1985. Sponsors have been reluctant to include them in their projects because they bring in less rent and are considered by some sponsors to be more difficult to market than one-bedroom units.

FMRs for efficiencies bring in less rent because the market rents on which they are based do not cover average total costs. The financial disincentive (loss in rents) caused by reduced project revenues could be overcome if HUD were to establish FMRs for efficiency units that reflect the savings in costs from building these units.

Sponsor perceptions that efficiency units are more difficult to market have not been borne out at all the projects we reviewed. Tenants have accepted these units in some cases, and do so especially when subsidized one-bedroom units have not been available. Tenant acceptance has been further enhanced by providing well-designed efficiency units.

Program costs also could be reduced by selecting more modest projects for funding. Modestly designed projects were not always selected because modest design's importance was diminished by the project's financial and operational capacity. HUD, however, could elevate modest design's importance by using a two-tiered system. Under this system, tier one projects, for example, with acceptable financial and operational capacity would compete for selection in tier two on the basis of modest design and project site costs.

## Agency Comments and Our Evaluation

In commenting on our report (see app. V), HUD stated that it has been studying, along with the Congress and program participants, various ways to address the financial feasibility issue with regard to development of efficiencies and the applicability of FMRS. HUD, however, disagreed with basing efficiency rents on the cost to construct and operate these units. It stated that this could lead to inflated costs, thus negating any cost savings. According to HUD, previous studies have shown that controlling the FMRs has been one of the Department's most effective ways of controlling section 202 project development costs.

As explained earlier, efficiencies are an anomaly in the private market, and therefore we believe it is questionable whether a reasonable FMR can be established for these units based solely on the market rents charged for them. Consequently, in seeking ways to address the financial feasibility issue associated with efficiencies, we continue to believe that some form of recognition will have to be given to the costs to construct and operate these units if this issue is to be resolved. We do not specify how rents should be adjusted but rather leave this decision to HUD's discretion. The ensuing rent standard, i.e., FMR, would continue to control development costs and, together with HUD's cost containment requirements, safeguard against inflated costs.

HUD disagreed that changes in its project selection process will produce cost savings. First, HUD stated that the additional costs to sponsors of preparing more detailed exhibits would far exceed the limited benefits, if any, from such a change. HUD stated that the exhibits it requires applicants to submit were designed to provide enough information to make an informed decision about whether selected projects might succeed, while minimizing front-end expenditures by nonprofit sponsors. More specifically, HUD stated that the required architectural exhibits are sketchy at best and are often not prepared by an architect. While these exhibits give HUD an idea of what the sponsor proposes to do, HUD stated that the level of detail is inadequate to perform a reasonable cost estimate.

As a second reason for disagreeing with changes in the project selection process, HUD stated that it informs selectees that they are responsible for developing a viable project and that their selection does not constitute HUD acceptance of the proposed design concept. Thus, according to HUD, it is able to impose any necessary design changes at later stages of processing.

By elevating the importance HUD places on a project's cost containment and modest design features in project selection, we are not suggesting that HUD should change its present requirements for exhibits. Nor are we suggesting that sponsors should be required to incur additional expenses in order to provide HUD with more detailed information on which to evaluate project costs. We consider the information HUD currently receives from sponsors adequate for making an informed decision on a project's cost containment and modest design features.

While the potential for cost savings is difficult to quantify, we believe the opportunity exists to achieve economies. For example, between two competing but similarly designed projects, the one containing more efficiency units and/or smaller one-bedroom units would clearly appear to be superior if the other project lacked these identical features. In our opinion, the construction of modest housing begins when sponsors first conceptualize their projects. We believe that by selecting those that are clearly modest in concept, HUD would minimize the need to impose subsequent design changes, which can be timely and costly to sponsors as well as HUD.

## Recommendations to the Secretary of Housing and Urban Development

To further control and reduce the cost of the section 202/8 program, we recommend that the Secretary of HUD should:

- Adjust rents for efficiencies to make these units more financially feasible for sponors to construct and operate.
- Change the project selection process to give greater consideration to costs. Specifically, HUD should elevate the importance of cost/modest design in project selection by utilizing a two-tiered approach whereby projects found acceptable in tier one on the basis of such factors as financial/operational capacities would compete for selection in tier two on the basis of modest design and project site cost commensurate with area needs.

# Program Assistance Benefits Low-Income Elderly, but Minority Participation Was Relatively Low

In 1981, over 4 million very low-income, elderly headed households needed housing assistance. Over 3 million of them were paying an excessive share of their income for housing, and more than 1 million lived in housing that was physically inadequate. HUD has allocated section 202/8 program funds among its field offices in a manner consistent with these needs.

Most program beneficiaries were single. Beneficiaries on average were 73 years old, had an annual income of $6,600, and received about $330 a month in section 8 rental assistance payments. While the program primarily has benefited very low-income elderly persons—those with incomes equal to or less than 50 percent of the median income (adjusted for household size) for the area—uncertainty exists as to how much the program is helping the elderly who previously lived in costly and/or inadequate housing. However, HUD has actions underway for selecting tenants that should help to direct program assistance to those with the greatest need.

Minorities have benefited less from the program than nonminorities, relative to their respective need for housing assistance. Minorities, which represent 22 percent of the elderly in need of housing assistance, accounted for 13 percent of the tenants. Of the minorities served, most were concentrated in a few projects. HUD is in the process of implementing a series of reporting requirements to strengthen its civil rights monitoring and enforcement efforts.

## Many Elderly People Need Housing Assistance

According to Annual Housing Survey data, 4.1 million very low-income, elderly headed households needed housing assistance in 1981.[1] Households were considered to need housing assistance if they lived in housing that was physically inadequate as defined by HUD (e.g., lacked plumbing or electricity; see app. III) or had a higher than acceptable housing cost burden. The latter includes renters who pay more than 30 percent of their income in rent and homeowners who pay more than 40 percent of their income for housing, excluding expenditures for maintenance and improvements. HUD used these percentages to determine the affordability of housing for lower income families.

[1]The AHS provides extensive information on housing units in the United States, including data on rent and other housing costs; income and other characteristics of households residing in the housing units; and indicators of housing quality, such as plumbing and kitchen facilities. The survey, authorized by the Housing and Urban Development Act of 1970, is performed through interviews by the Bureau of the Census. About 60,000 housing units are surveyed.

Of the very low-income, elderly headed households in need of housing assistance, 2.7 million had a higher than acceptable housing cost burden, 1 million lived in physically inadequate housing, and 400,000 resided in housing that was both physically inadequate and had an unacceptable cost burden. Most of those in need of assistance lived in urban areas (Metropolitan Statistical Areas), and most lived alone. Most in need were nonminorities and most were renters rather than homeowners.

Details are shown in table 4.1.

**Table 4.1: Housing Needs for Very Low-Income, Elderly Headed Housholds in 1981**

Dollars in Millions

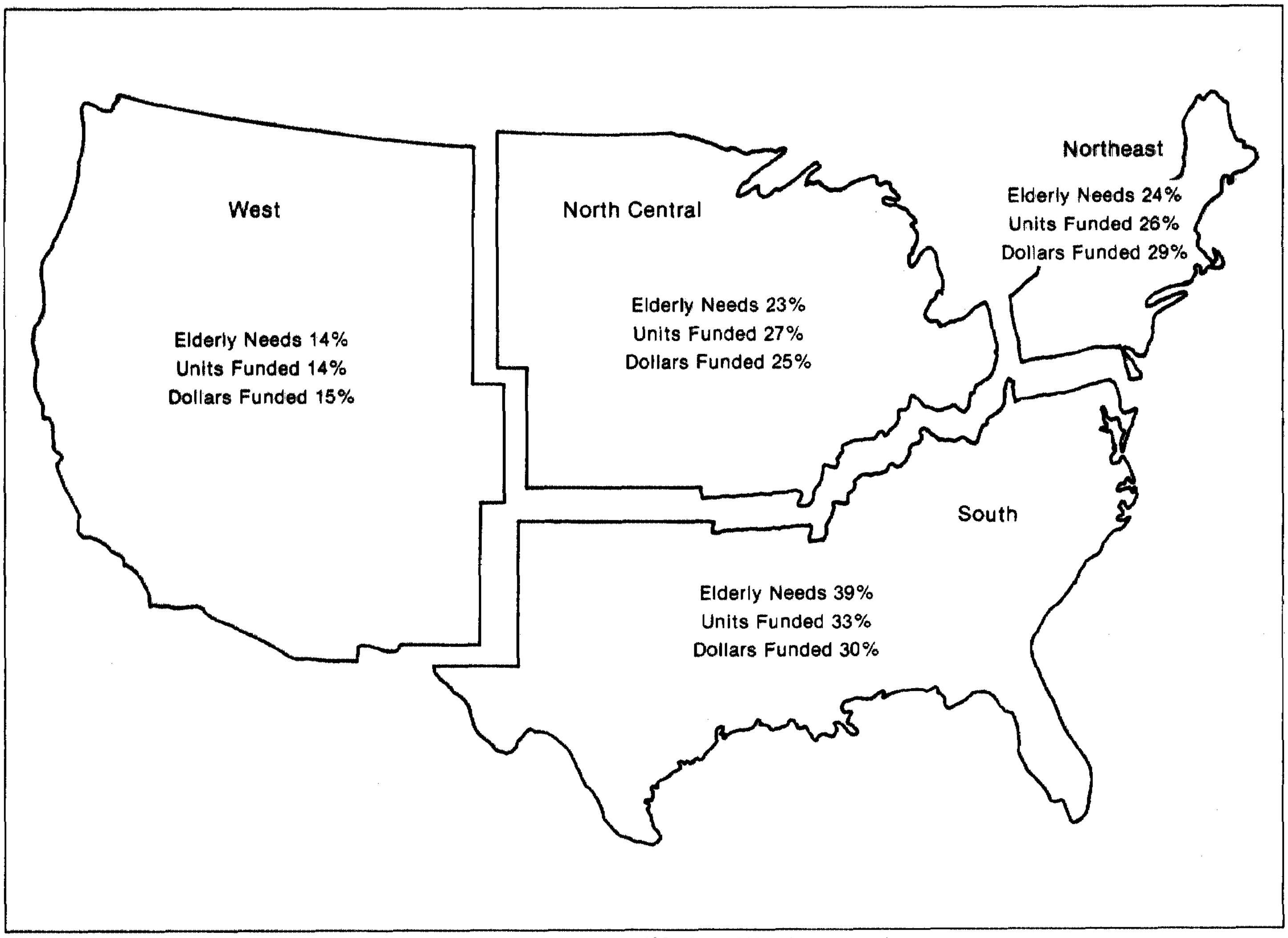
| | Basis for need | | | | |
|---|---|---|---|---|---|
| | Physical inadequacy only | Cost burden only | Inadequacy and cost burden | Total needs | Percentage |
| All very-low income elderly headed households | 1.0 | 2.7 | 0.4 | 4.1 | 100 |
| Urban | .4 | 2.1 | .2 | 2.7 | 66 |
| Nonurban | .6 | .6 | .2 | 1.4 | 34 |
| Homeowners | .7 | .9 | .1 | 1.7 | 41 |
| Renters[a] | .3 | 1.8 | .3 | 2.4 | 59 |
| Nonminority | .7 | 2.3 | .2 | 3.2 | 78 |
| Minority | .3 | .4 | .2 | .9 | 22 |
| Household size: Single person | .5 | 1.8 | .2 | 2.5 | 61 |
| Two or more | .5 | .9 | .2 | 1.6 | 39 |

[a]Renters paying cash for rent.

## HUD's Allocation/Use of Program Funds Generally Reflects Housing Needs of the Elderly

As shown in figure 4.1, HUD's allocation and use of section 202 loan funds for fiscal years 1982-84 generally reflected elderly housing needs on the basis of 1981 Annual Housing Survey data. Some disparity exists, most notably in the South, between elderly housing needs and the units or dollars funded under the section 202 program. However, we did not consider the disparity significant for two reasons. First, statistical variances in the Annual Housing Survey's housing needs data could account for such disparity. Second, HUD's definition of inadequate housing tends to overstate housing needs in the South. That is, HUD considers a unit physically inadequate if, among other things, it is heated with a space heater. Because the South relies more on such heaters than other regions, it tends to have a higher incidence of housing inadequacies for this reason. However, in a large percentage of these cases, space heaters may actually be adequate, considering the climatic conditions in the area.

**Figure 4.1: Comparison of Elderly Housing Needs With HUD's Allocation/Use of Section 202 Funds by Census Region, Fiscal Years 1982-84[a]**




Housing needs based on 1981 Annual Housing survey data.

In allocating section 202 funds among its field offices, HUD is required to consider, as far as practicable, the relative needs of areas and communities. These needs are reflected by data on population, poverty, housing overcrowding, amount of substandard housing, or other objectively measurable conditions.

Using data from the 1980 Census, HUD allocated fiscal year 1985 program funds on the basis of an equal weighting of the following factors:

- The total number of owner and renter elderly-headed households aged 62 or over that have very low incomes.
- The number of very low-income elderly renter households that (1) lack complete plumbing, (2) have more than one person per room, and (3) pay 30 percent or more of their income for rent.
- The number of persons having a public transportation disability, i.e., any health condition lasting more than 5 months that restricts or precludes the use of public transportation.

Although the first two factors duplicate the number of elderly renter households with housing deficiencies, HUD considers these households to have the greatest need for housing assistance, and expects these households to comprise the largest number of program beneficiaries. The last factor provides some measure of the needs of the handicapped population, which is also served by the section 202 program.

## Characteristics of Section 202 Beneficiaries

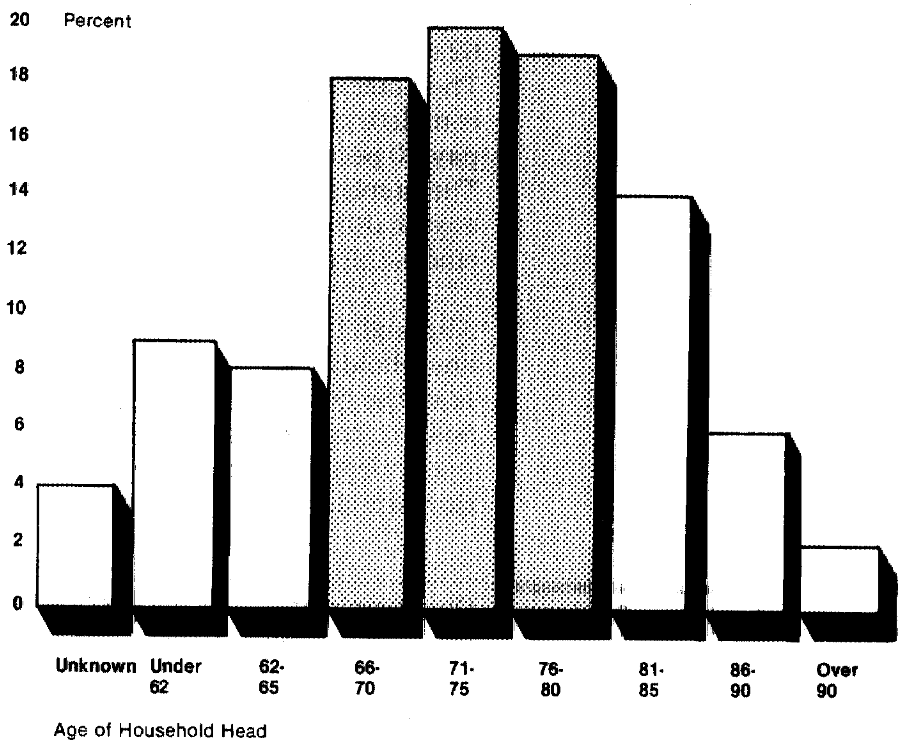
Our sample of 142 of the 1,274 section 202/8 projects constructed between February 1975 and January 1985 shows that the majority of program beneficiaries were single-person households. Beneficiaries on average were 73 years old, were white, had lived in their unit/project for about 2.5 years, and had an annual income of about $6,600 and modest assets. Moreover, most program beneficiaries (82 percent) had very low incomes—below 50 percent of the median income (adjusted for household size) for the areas in which they lived.

Most beneficiaries lived in a one-bedroom unit that rented on average for about $480 a month. The average beneficiary contributed about $146 toward this rent, and the balance of $334 was paid by the federal government through the section 8 rental assistance program. Additional details are presented in figures 4.2-4.4.[2]

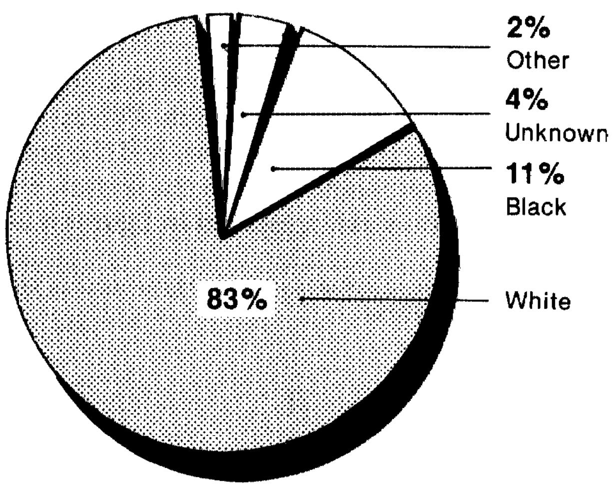
[2] Appendix IV shows the confidence intervals for key factors in our sample at the 95-percent confidence level.

**Figure 4.2: Demographic Characteristics of Program Beneficiaries, 1983-84**

Section 202 Beneficiaries Were Generally Between 66 and 80 Years Old...



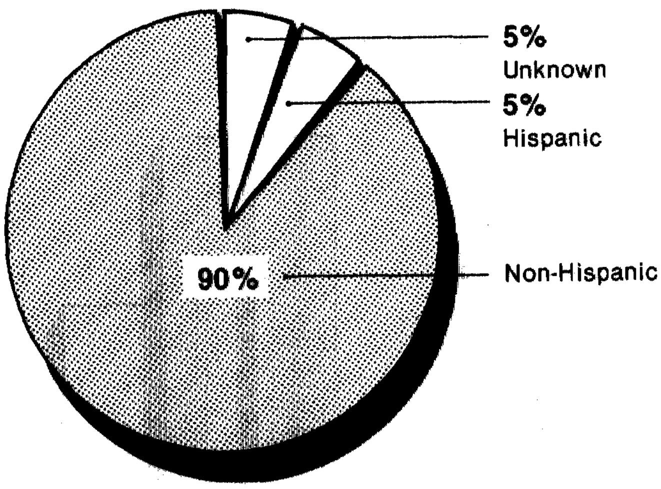

White . . .




Shaded areas for emphasis only.

**Figure 4.2: Demographic Characteristics of Program Beneficiaries, 1983-84** (Continued)

Non-Hispanic . . .




And Living Alone.

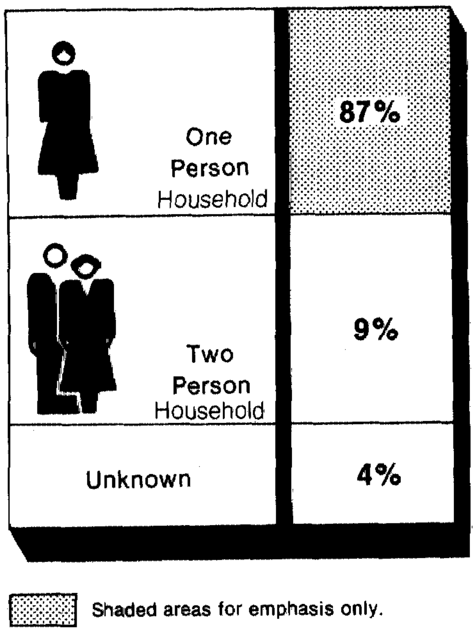
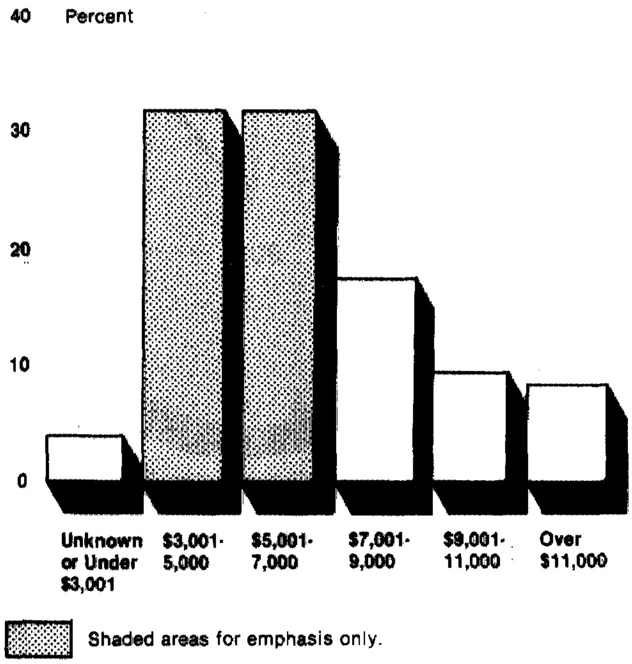


**Figure 4.3. Financial Characteristics of Program Beneficiaries, 1983-84**

Section 202 Beneficiaries Generally Had Incomes Between $3,000 and $7,000 . . .



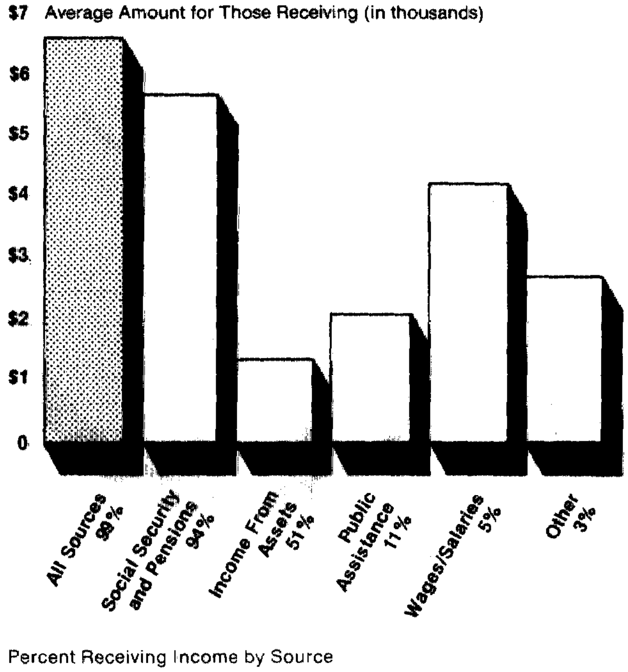

And Modest Assets.

| Assets | Beneficiaries: All | Beneficiaries: New[a] |
|---|---|---|
| $0 or Unknown | 59% | 39% |
| Under $5,000 | 20% | 28% |
| $5,001-$10,000 | 5% | 8% |
| $10,001-$25,000 | 8% | 12% |
| $25,001-$50,000 | 6% | 9% |
| Over $50,000 | 2% | 4% |

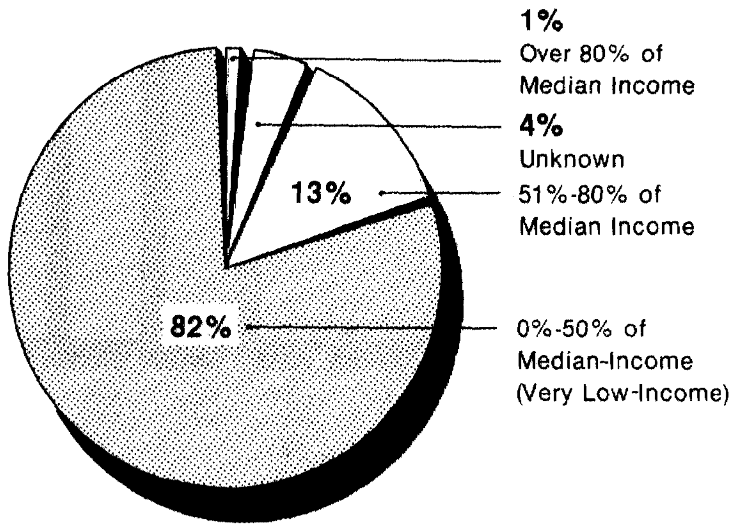
[a]Only new beneficiaries are required to report assets.

**Figure 4.3. Financial Characteristics of Program Beneficiaries, 1983-84**
(Continued)

Their Incomes Averaged $6,600, Largely From Social Security and Pensions . . .




And Most Had Incomes Equal to or Less Than 50% of the Median Income (Family Size Adjusted).




Shaded areas for emphasis only.

**Figure 4.4: Housing Characteristics of Program Beneficiaries, 1983-84**

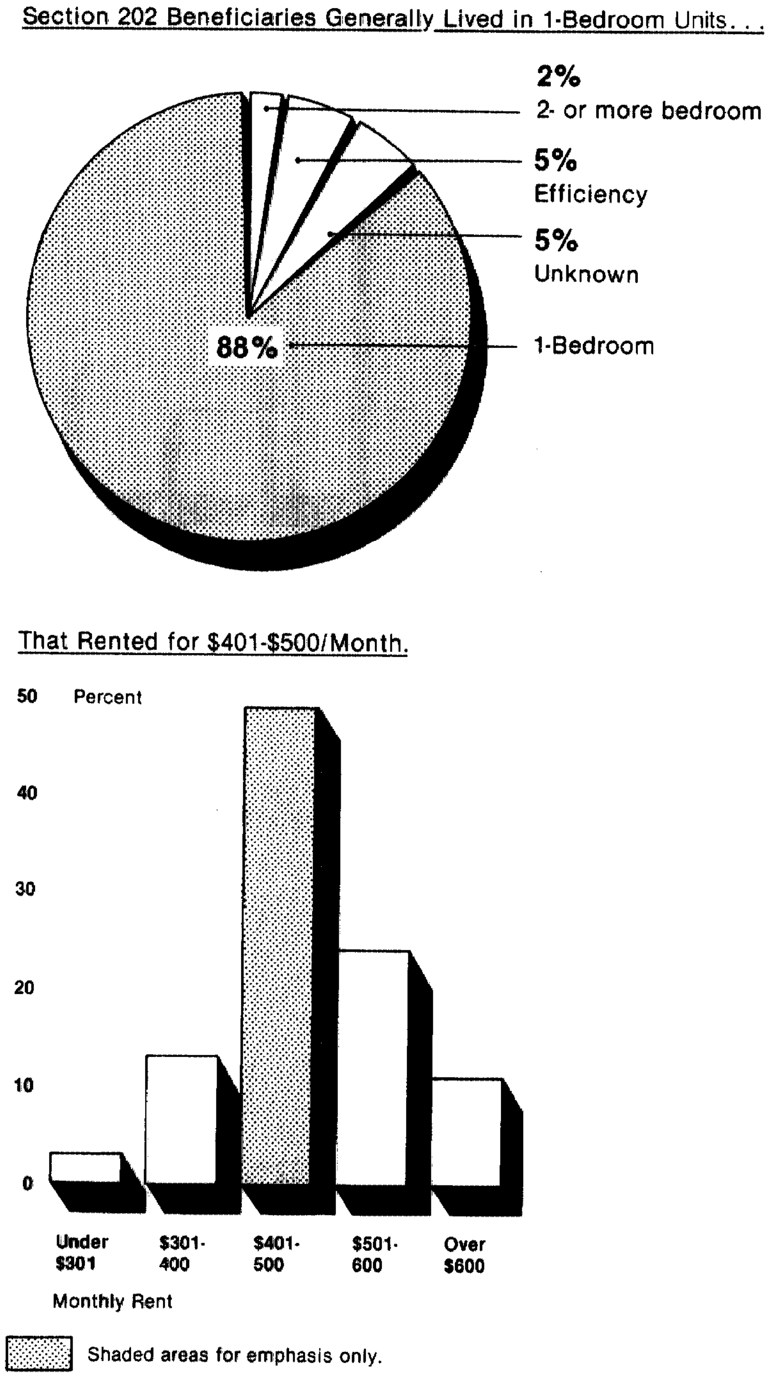
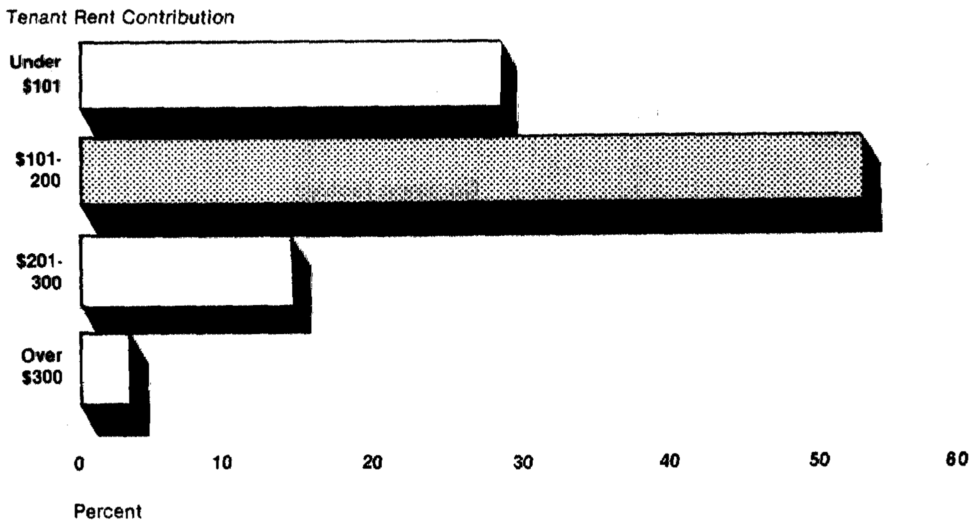
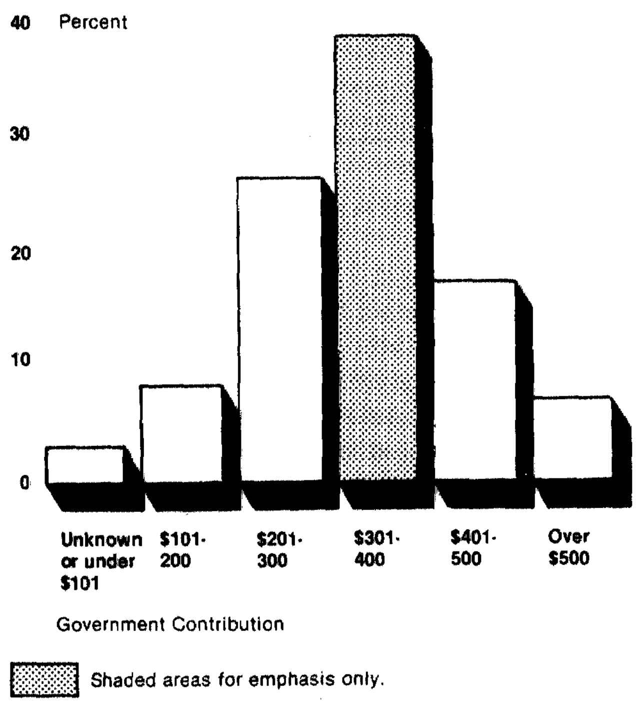


**Figure 4.4 Housing Characteristics of Program Beneficiaries, 1983-84**
(Continued)

Beneficiaries Generally Contributed $101-$200/Month Toward This Rent . . .




And the Government Generally Paid a $301-$400/Month Subsidy on This Rent.



Our sample of section 202/8 beneficiaries produced results similar to those reported by the Senate Special Committee on Aging in its 1983 survey of section 202 housing projects.[3] Table 4.2 compares the factors common to both surveys.

**Table 4.2: Comparison of Survey Results on the Characteristics of Beneficiaries**

| | Section 202/8 Beneficiaries | |
|---|---|---|
| Common factors | Special Committee on Aging's 1983 Survey[a] | GAO 1983-84[b] |
| Average age | 71 | 73 |
| Age distribution (in percent) | | |
| Ages | | |
| Under 62 | 9 | 9 |
| 62 - 65 | 10 | 8 |
| 66 - 70 | 18 | 18 |
| 71 - 75 | 20 | 20 |
| 76 - 80 | 25 | 20 |
| 81 - 85 | 11 | 14 |
| Over 85 | 7 | 8 |
| Unknown | | 3 |
| Percent single person households | 81 | 87 |
| Average income | $6,028 | $6,600 |
| Percent one-bedroom units | 91 | 88 |
| Average monthly rent contribution | $131 | $146 |
| Average monthly utility cost when paid separately | $33 | $30 |

[a]Represents responses from 739 project sponsors surveyed, or a 47- percent response rate.

[b]Statistical sample of 142 projects (100-percent response rate) containing 11,609 tenants.

## Uncertainty Exists About Whether Elderly With the Greatest Needs Are Being Served

Uncertainty exists as to whether those elderly with the greatest needs have been served by the program. Few of our sample program beneficiaries assisted under the section 202/8 program had previously lived in substandard housing or were involuntarily displaced at the time they received assistance under the program. In addition, HUD does not require project owners to collect and report data on the previous housing cost paid by program beneficiaries selected for admission. Consequently, we

[3]Special Committee on Aging, United States Senate, Section 202 Housing for the Elderly and Handicapped: A National Survey, Committee Print S. Prt. 98-257, December 1984.

could not determine the extent the program was serving elderly households that previously had an excessive housing cost burden. However, HUD has actions underway to address this question.

Of the 11,609 tenants in our sample of 142 section 202/8 projects, 2,196, or about 19 percent, were new tenants who moved in between 1983 and 1984. Of the 2,196 new tenants in our sample, 4 percent had previously lived in substandard housing and an additional 6 percent were about to lose their housing. Further, less than 1 percent had been displaced by government action or natural disasters, and only 8 percent had been displaced through private actions. (We considered only new tenants (beneficiaries) because only new tenants are required to report on their previous housing conditions or displacement status.)

In 1979, the Housing Act of 1937 was amended to require project owners participating in the section 8 new construction program, which includes projects built under the section 202 program, to give a preference in tenant selection to families that occupy substandard housing or are involuntarily displaced at the time they are seeking housing assistance. These provisions were expanded in the 1983 amendments to require that a preference also be given to selecting families who pay 50 percent or more of their income in rent. On September 26, 1984, HUD issued proposed regulations to implement the preference requirements of the 1979 and 1983 amendments for comment. However, because of numerous changes to the proposed regulations, HUD plans to reissue them for comment in 1986, which will delay issuance of final regulations.

At the time we visited projects, sponsors were not required to comply with these preference requirements. Nevertheless, we discussed tenant selection practices with project owners or managers at 25 of the projects we visited to determine the extent to which project sponsors were initiating preferential selection consistent with the act's amendments. Nineteen of the sponsors stated that they selected tenants on a first come, first served basis if tenants meet HUD's income eligibility requirements. Only six stated that they considered the individuals' or families' housing conditions in selecting tenants.

In March 1985, HUD revised its occupancy management handbook to require project owners to give preference in tenant selection to families who were living in substandard housing or who were involuntarily displaced. The rent burden preference added by the 1983 amendments was not included in the handbook, but HUD expects to add it later, after its regulations are finalized.

## Minority Beneficiaries Were Underrepresented

HUD requires section 202/8 project owners to comply with their HUD-approved Affirmative Fair Housing Marketing Plan. The plan outlines the marketing and outreach strategies to be followed in selecting tenants for the project, including special marketing efforts to attract persons who are least likely to apply because of such factors as the racial and ethnic residential composition of the neighborhood in which the project is located. The plan is designed to promote equal housing choice for all prospective tenants regardless of race, color, religion, creed, or national origin. HUD requires owners to monitor the results of their marketing efforts and to adjust their marketing techniques as necessary to attract the applicant mix specified in the plan.

At the 142 projects sampled, minorities accounted for 13 percent of the program beneficiaries. (See p. 54.) However, according to Annual Housing Survey data, minorities accounted for 22 percent (see p. 51) of the 4.1 million very low-income, elderly headed households in need of better housing in 1981.

Most projects among the 142 we sampled had few, if any, minorities.[4] As shown in table 4.3, we found that

- 42 percent of the projects, which housed about 33 percent of the tenants, had no minority tenants and
- 70 percent of the projects, which had 68 percent of the tenants, had 5 percent or fewer minority tenants.

Additional details are also shown in table 4.3.

[4]Sixty-eight percent, or 97, of the projects sampled were located in urban (metropolitan) areas.

**Table 4.3: Distribution of Projects by Percentage of Minority Tenants**

| Percentage of minority tenants | Projects Number | Projects Percent | Percentage of total tenants sampled served by projects |
|---|---|---|---|
| 0 | 59 | 42 | 33 |
| Over 0 - 2 | 20 | 14 | 18 |
| Over 2 - 5 | 20 | 14 | 17 |
| **Total** | | **70** | **68** |
| Over 5 - 10 | 9 | 6 | 6 |
| Over 10 - 15 | 4 | 3 | 3 |
| Over 15 - 25 | 8 | 6 | 5 |
| Over 25 | 22 | 15 | 18 |
| **Total** | **142** | **100** | **100** |

For the most part, minorities were concentrated in a few projects. Sixty percent of the minorities in our sample were housed in 13, or 9 percent, of the projects sampled. At each of the 13 projects, more than 50 percent of the tenants were minorities.

We did not review the adequacy of Affirmative Fair Housing Marketing Plans and/or the effectiveness of project owners in implementing these plans. This matter was beyond the scope of our review. In addition, because our analysis of tenant data was not completed until after most of our field work was finished, we were not aware of the low minority participation soon enough to consider this matter more fully. Nevertheless, because of the high proportion of projects with few or no minorities, we discussed with HUD officials the results of our analysis and the adequacy and effectiveness of Affirmative Fair Housing Marketing Plans for section 202 projects.

In response, HUD officials told us that they were aware that problems exist in serving elderly minorities. While HUD officials were not aware of the problem's magnitude within the section 202 program, HUD officials stated that our data provided some measure of the problem. They stated, however, that other important factors, such as project location and the racial/ethnic mix of the community served, also needed to be considered. HUD officials agreed that our data did suggest that there was a need for HUD to examine the implementation of Affirmative Fair Housing Marketing Plans, as well as tenant selection practices.

Besides sharing our concern, HUD officials stated that HUD was in the process of instituting a series of reporting requirements to provide data on tenants and applicants for HUD-assisted projects, including section 202/8 projects. These requirments are designed to strengthen HUD's civil rights monitoring and enforcement efforts. Three of the proposed reports are designed to allow HUD to monitor the implementation of Affirmative Fair Housing Marketing Plans and tenant selections, and to target its civil rights monitoring and compliance review activities.

According to HUD officials, HUD's civil rights efforts in recent years have been devoted primarily to HUD's public housing program, which provides over a million housing units for low-income families. HUD officials, however, stated that after their proposed data collection system is implemented, HUD will be in a position to consider shifting and/or increasing its resources to address problems in other HUD programs/projects.

## Conclusions

Millions of very low-income elderly people live in costly and/or substandard housing and therefore have a need for the assistance provided by the section 202/8 program. Although HUD has distributed program funds in a manner that adequately reflected these needs, uncertainty exists as to whether those elderly with the greatest needs have benefited from the program. HUD, however, has actions underway to address this uncertainty.

Considering the low level of minority participation at most of the projects we sampled, HUD needs to do more to ensure that program assistance is extended to minorities. HUD is attempting to institute a series of reporting requirements to strengthen its civil rights monitoring and compliance activities, which should provide the agency with more information on programs and projects requiring its attention.

# Section 202 Processing Stages

## Preapplication Stage

This phase begins when an applicant (borrower), contacts the HUD field office and expresses interest in developing a project. The HUD field office takes the name and contacts the borrower when funds are available and the field office is in a position to advertise. After HUD advertises, the application period begins. In this period, the applicant

- selects a development team,
- locates a site,
- obtains site control, and
- forms a nonprofit borrower corporation and applies for an IRS tax exemption.

## Fund Reservation Stage

This stage begins when the borrower submits its application for a section 202 fund reservation. Applications are reviewed to determine applicant eligibility and capacity in developing housing for the elderly or handicapped consistent with prescribed statutory and program criteria. During the fund reservation stage, HUD conducts

- initial screening for completeness,
- preliminary evaluation (threshold criteria),
- technical processing, and
- rating and ranking for selection.

HUD uses the following criteria for selecting a project:

- Borrower's capacity (experience).
- Financial capacity.
- Location.
- Modest design/cost.
- Other.

## Conditional Commitment Stage

### Preapplication Action

The borrower's architect works closely with the HUD design representative during preparation of preliminary plans. Technical processing decisions made at this stage include

- acceptability of design and minimum property standards (MPS) compliance,
- estimated cost of the project,
- "as is" and fully improved value of the site,
- estimates of operating expenses,
- supportable construction costs,
- financial and credit acceptabilty of general contractor,
- acceptability of contract rents, and
- determination of loan amount and estimated cash requirements for borrower.

## Firm Commitment Stage

Technical processing includes

- review of final contract drawings and specifications and
- reanalysis of underwriting determinations if changes to proposal are made.

## Initial Loan Closing

- Borrower's attorney prepares initial closing documents.
- Borrower escrows minimum capital investment and contractor obtains building permit.
- Construction commences after formal loan closing with the first loan (draw) disbursement and recordation of mortgage.
- Typically, a preconstruction conference is held to discuss labor standards, prevailing wages required, and other HUD policy.

## Construction Stage

- Management agent begins marketing (90 days prior to initial occupancy).
- Project is substantially completed and management agent obtains permission to occupy the project from HUD field office and local government.

## Post-Construction

- Management agent starts renting units.
- Borrower and contractor submit cost certification.
- Borrower and HUD execute section 8 housing assistance payments contract.

## Final Closing

- Cost certification determines maximum mortgage on the basis of actual cost of completed project.
- Borrower's attorney prepares final closing documents.

# Section 202 Cost Containment Supplemental List, May 1983

1. Eliminate parapets and other unnecessary projections or breaks at roofs. Flashing and counterflashings are expensive to build and to maintain during occupancy. Investigate the use of membrane (rubber) roofing in lieu of a build-up roof.

2. Single width masonry wall construction is acceptable if properly flashed to prevent the penetration of moisture. Nonbearing veneers should be aluminum/vinyl siding or plywood.

3. Limit the number of elevators. Check elevator design for costly features such as excess speed and unnecessary control. Cab and door design should be baked enamel.

4. Lightweight concrete floor topping is excessively costly. Carpet is an effective sound control.

5. Eliminate decorative door sidelights and transoms.

6. Do not provide air conditioning in cool climates (northern zones particularly) especially in units for the elderly.

7. Parking lots should be efficiently designed as close as possible to buildings, with no excess parking spaces or roadways. Both parking lots and sidewalks should be paved with bituminous concrete in lieu of portland cement concrete. Use precast concrete at islands and protrusions. Curbs and bumpers should be bituminous concrete or railroad ties.

8. Ceiling heights should be a maximum of 8 feet from floor to ceiling.

9. Bathroom lights and outlets should be integral to medicine cabinets or ceiling fans, eliminating the need for a separate fixture.

10. Closet doors should be full height—where possible, full width—metal bifold in lieu of bypassing wood, thus elminating dry-wall headers and stub partitions.

11. Hose bibs should be used in place of yard hydrants.

12. Site lighting can be accomplished by building mounted fixtures rather than free-standing poles and fixtures.

13. Sheetrock may be fastened directly to wood joists instead of to furring channels or strapping. At metal joists, attach sheetrock to metal strapping without suspension.

14. Ceramic tile should be used only in the tub and shower enclosures. The remaining areas should be painted. Epoxy paint may be used in lieu of ceramic tile.

15. Ductless hoods may be used instead of ducted hoods unless there is a requirement for mechanical ventilation.

16. Where possible, use one or two large windows in place of two or three smaller ones.

17. Eliminate finish in stairwells (except in primary stairwell), mechanical rooms, and other utility areas.

18. Specify 5/8-inch sheetrock only to meet code requirements.

19. Specify residential hardware except in common areas.

20. Avoid costly items such as elaborate signs and directories, stainless steel brackets, and railings.

21. Minimize landscaping.

22. Electrical fixtures and plumbing trim should be minimum and not extravagant.

23. In smaller buildings, a gable roof should be used in lieu of a flat roof.

24. One- or two-story protrusions to high-rise buildings are costly and should be avoided.

25. Underground or covered parking should be avoided except in extreme cases where no alternative exists to meet local requirements. Excessive local requirements should be appealed.

26. Large, elaborate, and extensive entrances and elevator lobbies should be avoided.

27. Excessive common areas must be avoided. Common areas exceeding 5 percent of net rentable space must be investigated completely by the

area office staff with an eye to eliminating them. The 5-percent calculation will include the lobby, common kitchen and dining areas, meeting and recreational areas, tenant workshops, etc. This calculation will not include mechanical rooms, managers' units, and small offices or halls.

28. Commercial areas must support market rates that service the prorata share of cost and expenses. Otherwise, these areas must be included in the common area calculation.

29. If the sponsor includes design features and amenities that exceed the intent of cost containment and proposes to pay for excess costs, the payment must take into consideration any excess maintenance costs associated with the excess design. Payments by the sponsor that originate from HUD by way of Block Grants or Urban Development Action Grants cannot be accepted as justification for exceeding the modest design criteria.

# HUD Criteria for Inadequate Housing

| Type of deficiency | Description of deficiency |
|---|---|
| Plumbing | Lacks or shares some or all plumbing facilities. The unit must have hot and cold piped water, a flush toilet, and a bathtub or shower—all inside the structure and for exclusive use of the unit. |
| | Lacks adequate provision for sewage disposal. The unit must be connected with a public sewer, spetic tank, cesspool, or chemical toilet. (Units with this deficiency are almost invariably defined as having a plumbing deficiency as well.) |
| Kitchen | Lacks or shares some or all kitchen facilities. The unit must have an installed sink with piped water, a range or cookstove, and a mechanical refrigerator—all inside the structure and for exclusive use of the unit. |
| Physical structure | Has three or more of five structural problems: leaking roof, open cracks or holes in interior walls or ceiling, holes in the interior floors, either peeling paint or broken plaster over 1 square foot of an interior wall, and evidence of mice or rats in the last 90 days. |
| Common areas | Has three or more of four common area problems: no light fixtures (or no working light fixtures) in common hallway; loose, broken, or missing stairs; broken or missing stair railings; and no elevator in building (for units two or more floors from main building entrance in buildings four or more stories high). |
| Heating | Has unvented room heaters which burn oil or gas. If unit is heated mainly by room heaters burning gas, oil, or kerosene, the heaters must have flue or vent. |
| Electrical | Lacks electricity. |
| | Has three out of three signs of electrical inadequacy: one or more rooms without a working wall outlet, fuses blown or circuit breakers tripped three or more times during last 90 days, and exposed wiring in house. |

# Section 202 Program Beneficiaries

**Table IV.1: Confidence Intervals for Selected Items Sampled at 95-Percent Confidence Level**

| Item | Mean | Lowest | Highest | ± Interval |
|---|---|---|---|---|
| Age | 73.3 | 72.0 | 74.6 | 1.3 |
| Percentage:<br>Nonminority | 82.8 | 78.4 | 87.2 | 4.4 |
| Minority | 13.0 | 8.6 | 17.4 | 4.4 |
| With incomes 50% or less of median | 82.3 | 80.3 | 84.2 | 2.0 |
| Annual income | $6,600 | $6,396 | $6,804 | $204 |
| Wages and salaries | $4,141 | $3,729 | $4,552 | $411 |
| Social security and pensions | $5,686 | $5,541 | $5,831 | $145 |
| Public assistance | $2,061 | $1,845 | $2,278 | $217 |
| Income from assets | $1,318 | $1,185 | $1,449 | $132 |
| Utility allowance | $ 30 | $ 26 | $ 35 | $ 4 |
| Gross rent | $ 482 | $ 464 | $ 499 | $ 18 |
| Gross family contribution | $ 146 | $ 141 | $ 151 | $ 5 |
| Assistance payment | $ 377 | $ 320 | $ 354 | $ 17 |

# Comments From the Department of Housing and Urban Affairs

Note: GAO comments supplementing those in the report text appear at the end of this appendix.

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, D.C. 20410-8000

June 19, 1986

OFFICE OF THE ASSISTANT SECRETARY FOR
HOUSING-FEDERAL HOUSING COMMISSIONER

Mr. J. Dexter Peach
Director, Community and Economic
Development Division
United States General Accounting Office
Washington, DC 20548

Dear Mr. Peach:

Your letter of May 1, 1986, addressed to the Secretary of Housing and Urban Development transmitting a proposed report to the Congress entitled: "Elderly Housing: HUD's Cost Containment Program Could Be More Effective," has been referred to me for reply.

For the purpose of clarification and accuracy, the following points are called to your attention and page and table numbers refer to those in your report.

See comment 1.

1. Under the Fiscal Year 1985 HUD Appropriation Act, Congress provided a loan authority limitation of $600 million for the Section 202 Direct Loan Program (page 21). Of this amount, $557.7 million was used to reserve 12,416 units. The balance was used for amendment purpose to take care of loan increases required for units reserved in earlier years. It should be noted that loan authority reserved at the reservation stage is based strictly on a formula computed on the proposed unit makeup and structural system (i.e., elevator or nonelevator). To reflect a true comparison of cost savings, the figures in the report should be based on cost certified figures after project completion rather than loan authority reservation amounts.

See comment 2.

2. Two bedroom units are prohibited for nonhandicapped elderly projects (Table 2.1) except for the resident manager's unit.

See comment 3.

3. On page 12, a comment is made about the similarity between conditional commitment and firm commitment processing. While it may appear that the two phases are the same with the exception of the level of detail of the contract documents, there are, in fact, legitimate reasons for this phased processing. We believe the conditional commitment phase is critical and have issued Notice 86-8 (copy enclosed) that seriously restricts a Field Office's authority to allow a Borrower to bypass the conditional stage. It is at the conditional stage that we get our first real opportunity to review the project design before considerable

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monies are expended for the preparation of final plans and specifications. Often we are able to require design changes that would produce cost savings that could not otherwise be realized at a later stage of processing. (The potential savings attributable to design changes are frequently lost when suggestions are made at the firm commitment stage due to increases in construction costs while redesign is underway.) Further, the conditional stage is the first point at which HUD has an opportunity to develop its cost estimate, which allows us to determine whether the project as designed will be feasible within the allowed budget.

See comment 4.

4. On pages 27 and 28 is a discussion of exemption from HUD's supplemental cost containment guidelines. We acknowledge that instructions in effect at the time this report was being developed did permit a waiver of cost containment guidelines if the rents were at or below 100 percent of the applicable Fair Market Rent (FMR); we point out that, in most cases, the costly features such as those identified in the report were paid for by the Borrowers from other than Section 202 loan proceeds. Consequently, elimination of these features would not necessarily have reduced costs to the Government in either Section 202 loan authority or Section 8 contract and budget authority. We also point out that Headquarters has taken an additional step through its management plan for its Field Offices to contain costs on Section 202 projects. The management plan requires that at least 10 percent of Section 202 projects (excluding group homes) for which an Agreement to Enter into a Housing Assistance Payments Contract is executed or amended during the Fiscal Year must have rents at or below 100 percent of the applicable FMR.

I will answer the recommendations in the order that they are presented in the report.

Recommendation No. 1: The Secretary of HUD, in order to provide greater consistency in the application of cost containment, should (1) specify that its supplemental guidelines are to be applied to all projects and (2) select a sample of projects for compliance review from each of the Field Offices. In addition, the Secretary should reexamine whether HUD's policy of allowing waivers to its efficiency requirement should be continued.

See comment 5.

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Reply: Part (1) of the recommendation has already been implemented. The Department issued Notice H-86-8, Cost Containment and Modest Design Requirements for Section 202, on April 2, 1986. This Notice (copy enclosed) states that cost containment and modest design requirements apply to all projects regardless of the proposed FMR level. The Notice also requires each Field Office to objectively examine every proposal to assure cost efficient design and provides guidance to assist in the analysis of project design to assure compliance with the Department's cost containment objectives.

Training based on this Notice will be given to our Field Offices during June 1986.

Part (2) of the recommendation is currently being addressed through Headquarters' ongoing monitoring of our Field Offices. To date in Fiscal Year 1986, on site Field Office reviews have been conducted in Minneapolis, New Orleans, Newark, Pittsburgh, Los Angeles and San Francisco with specific emphasis on the review of Section 202 projects in the design stage for compliance with cost containment objectives. We find this type of review to be superior to having Field Offices ship selected exhibits for Headquarters' review since the entire processing file is available and Field Office staff can be questioned on different matters. Training, too, can be conducted on the spot when deficiencies are discovered.

As to HUD's policy of allowing waivers to the efficiency requirement (Part (3) of the recommendation), we believe in retaining the waiver option, for there could be circumstances involving serious resistance to the efficiency units. The fact that Section 202 projects are subsidized by Section 8 rental assistance does not guarantee that all units will be easily marketed as evidenced by serious rent-up problems that we are beginning to witness in different parts of the country. However, we do recognize that the waiver provision could be strengthened and, therefore, we will rescind Field Office authority to grant such waivers, and grant them only in Headquarters. This will be implemented in Fiscal Year 1987.

Recommendation No. 2: To further control and reduce the cost of the Section 202/8 program, the Secretary of HUD should:

-- Adjust rents for efficiencies to make these units more financially feasible for sponsors to construct and operate.

-- Change the project selection process to give greater consideration to costs. Specifically, HUD should elevate the importance of cost/modest design in project selection by utilizing a two-tiered approach whereby projects found acceptable in tier one on the basis of such factors as financial/operational capacities would compete for selection in tier two on the basis of modest design and project site cost commensurate with area needs.

Reply: The Department, the Congress and program participants have been studying various ways to address the financial feasibility issue with regard to development of efficiencies and the applicability of Section 8 New Construction/Substantial Rehabilitation FMRs to the Section 202 program where the loan amount is based, in part, on what it costs to build the project. The Section 8 FMRs, prepared by our Field Offices, reflect what a tenant would be willing to pay for an unsubsidized unit of modest design. That market rent is influenced by factors other than the cost of building the unit. In areas with high vacancy rates, for example, it is the tenant who has the advantage and rents may not be sufficient to support the cost of new construction due to the oversupply of affordable housing units.

Frankly, we disagree with the proposal to base fair market rents on cost. Such a proposal could very well lead to inflated costs and defeat the purpose of the recommendation. Previous studies have shown that controlling the FMRs has been one of the Department's most effective ways of controlling Section 202 project development costs. We will, however, continue to explore options with regard to the financial feasibility and marketability of efficiencies.

We disagree that the second part of the recommendation will produce any cost savings. Because of the considerable interest that exists among Section 202 sponsors in competing for the limited loan authority available under this program, we have designed the required application exhibits so that they provide us with enough information with which to make an informed decision on the likelihood of success of the selected project while at the same time minimizing the front-end expenditure of funds by these nonprofit sponsors. Therefore, the architectural exhibits that are submitted are sketchy at best and are often not prepared by an architect. They simply give us an idea of what the sponsor proposes to do. The level of detail of the exhibits is inadequate to perform a reasonable cost estimate. Further, we state in Item 4 of our notification of selection letter, "It is understood that this letter places upon the Borrower the responsibility to develop a viable project and does not constitute acceptance of the proposed design concept . . . Therefore, the Section 202 and Section 8 reservations may be reduced or increased, as appropriate, based on firm commitment processing. . . ." This language was inserted in the approval letter to assure that selectees were aware that HUD could and would later impose changes to the design submitted at the fund reservation stage, if necessary.

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We believe that the costs to the sponsors of preparing exhibits to the level of detail that would be necessary to implement this recommendation far exceed the limited benefits, if any, that would be realized from its implementation.

Very sincerely yours,

Silvio J. DeBartolomeis
General Deputy Assistant Secretary

Enclosure

The following are GAO's comments on the Department of Housing and Urban Development's letter dated June 16, 1986.

## GAO Comments

1. We used $600 million only to illustrate the dollar magnitude of savings attributed to cost containment. Whether one uses $600 million or $557 million, given the impact of cost containment (14 to 16 percent reduction in costs per unit), we estimate HUD still would have needed about $100 million more without cost containment to fund the 12,400 new units approved in fiscal year 1985. We would have used cost-certified data but these data for fiscal year 1985 funded projects will not be available for several years when project construction is completed.

2. The report has been modified to reflect the use of two-bedroom units for the project managers' units.

3. We modified the report to reflect the importance HUD places on the conditional commitment phase.

4. At the offices we reviewed, section 202 loan proceeds were used to finance costly features included in projects having rents of 100 percent or less of fair market rents. But HUD instructions issued on April 2, 1986, which require all projects to adhere to HUD's guidelines, should resolve this problem. The report has been modified to reflect HUD's use of management plans to further contain costs.

5. In view of HUD's actions to implement our proposal, we are no longer making this recommendation in our report.

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