

Building Our Houses: Public Housing and Section 8 at the Crossroads¹

Introduction

The federal public housing program was created in 1937 in the depths of the Great Depression. At that time, the program's principal goals were to clear slums, create jobs and expand the supply of affordable housing for unemployed and underemployed American workers. Public housing did not solve the economic problems of the Great Depression, but it was one part of a larger national effort.

How have social and economic conditions changed today? FNMA (Fannie Mae) held a conference at the turn of the millennium and called for papers on the challenges ahead. The consensus of the responders was that the biggest challenge facing American society in the 21st century is the growing disparity of income and wealth. Wages for the lowest 20 percent of the population have declined in real terms since 1980 (with a brief and only temporary reversal at the end of the 1990s), and have been nearly stagnant during this time for much of the middle class. Public housing authorities (PHAs) cannot solve all of these problems, but they can be one part of a larger national effort.

The Harvard Joint Center for Housing Studies issues a report each year called *The State of the Nation's Housing*. Each year this report finds that the supply of private market rental housing that is affordable to low-income Americans is shrinking in absolute terms, and that the rent-income ratio of lower-income Americans (the percentage of their income they pay for housing) continues to grow. Most very low-income Americans (those with less than 50 percent of the area median income) now pay more than 50 percent of their income for housing. The recognized standard is 30 percent.

At the federal level, the picture is not encouraging. The federal income tax code continues to subsidize middle and upper class homeownership to the tune of over \$100 billion a year, through the mortgage interest and local property tax deductions. The government-sponsored enterprises (GSEs) like FNMA and FHLMC (Freddie Mac) help reduce housing costs for middle-income homebuyers. The Low Income Housing Tax Credit (LIHTC) enjoys strong support, but tax-credit developments house primarily households with over 50 percent

¹The following was adapted from a paper prepared by Wayne Sherwood for a recent meeting of the board of the Public Housing Authorities Directors Association (PHADA) held in Washington State. The views expressed are the author's and do not necessarily reflect those of the National Housing Law Project.

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of area median income (AMI). HUD continues to tout homeownership, even though homeownership is not feasible for everyone.

Since the 1994 elections, federal outlays for public housing have shrunk in real (inflation-adjusted) terms. The funding available a decade ago for the public housing stock as a whole for routine operations, maintenance and modernization (not counting HOPE VI) comprised: the operating fund at about \$3 billion, the capital fund at about \$3.3 billion, and Public Housing Drug Elimination Program (PHDEP) at \$300 million, a total of \$6.6 billion. Today the operating fund is about \$3.5 billion, the capital fund about \$2.8 billion, and there is no PHDEP program, a total of \$6.3 billion. If the total had grown by 2 percent a year for 10 years, that amount would now be \$8 billion. *In inflation-adjusted dollars the annual funding that is available generally to all PHAs is now 20 percent lower than it was a decade ago.* While it is true that over 100 public housing authorities have received HOPE VI revitalization grants during that time, this has done nothing to ease the pain of the other nearly 3,000 PHAs.

PHAs should be able to choose to serve a broader range of incomes, but the flow of federal subsidies under the public housing and Section 8 programs should continue to be targeted entirely to those households with under 50 percent of AMI.

Apart from HOPE VI, public housing now receives about \$6.3 billion a year, or about \$5,040 per unit per year. In contrast, the latest Congressional Budget Office (CBO) estimates are that housing choice vouchers will probably cost the federal government nearly \$7,000 per unit per year in Fiscal Year (FY) 2004, almost 40 percent more per unit than public housing. And public housing lasts longer. Yet the Office of Management and Budget (OMB) continues to claim that vouchers are cheaper. OMB's claim is wrong and needs to be vigorously rebutted.

I do not think that the average voucher amount should be reduced. Public housing spending should be increased. If public housing were given \$6,500 per unit for the total of the operating and capital fund for FY 2004, that would come to \$8.1 billion, nearly 30 percent higher than is currently expected. I think that would be completely reasonable.

I do not know whether there is any future for public housing or for PHAs. Given increasing budgetary pressures on domestic discretionary programs, I would say that it looks very bleak.

Some have suggested that the only rational course of action is for PHAs to cut loose from the federal government, go their own way and try to survive by raising rents, upscaling the income of their tenant populations, and housing middle

income residents instead of the poor. They can make their own case.

I agree that PHAs should be able to choose to serve a broader range of incomes, *but* I think that the flow of federal subsidies under the public housing and Section 8 programs should continue to be targeted entirely to those households with under 50 percent of AMI—*i.e.* “very low-income” people (with a large proportion of that funding going to those under 30 percent of AMI—*i.e.*, “extremely low-income” people).

I have written this paper not to rehash the current bad news, nor to try to predict where we are most likely to go in the near future (I don't know), but as an expression of my hopes about where we can go in the longer term.

Large and Growing Need for Affordable Housing for Many Different Groups of Very Low-Income Americans

The need for affordable housing for very low-income Americans has never been greater. These needs have been documented in a variety of reports such as:

- *The State of the Nation's Housing*, issued annually by the Harvard Joint Center for Housing Studies; and
- reports on America's housing needs by HUD's Office of Policy Development and Research, the National Low Income Housing Coalition, and the National Housing Conference.

In addition, newspaper articles from around the country have documented severe and growing needs for affordable housing by very low-income Americans.

There are many different groups of Americans who have different types of needs.

The Working Poor

One of the biggest needs for affordable housing is in the area of working people who have low-wage jobs. Households in this group who have or are seeking low-wage jobs need affordable housing that is close to these jobs, and that is decent, safe and sanitary. Increasingly, such jobs are in suburban areas. Households in this situation cannot afford to stay on public housing waiting lists for years. They need housing close to work. In dealing with this group of people, it is also necessary to take into account the growing racial and ethnic diversity of America's households, and how this affects their housing needs. The idea of partnering is important here, *e.g.* looking for ways in which urban PHAs can channel federal subsidies to community development corporations (CDCs) and nonprofits in the suburbs to help them develop low-income housing for low-wage working people.

The Low-Income Elderly and Frail Elderly

A second major group is the low-income elderly. A large percentage of our present elderly population have some savings and are homeowners. The private market will respond to much of this need.

“Asset Management”

However, there is also an unprecedented demographic wave of the elderly coming along in the form of aging Baby Boomers. There will be a growing demand for affordable elderly housing for those in this group who have substantially below-average financial resources.

The elderly are living longer, too, and there is a need for more options for “frail elderly” persons who could continue to live outside of nursing homes if they had adequate support.

Right now, public housing is probably not the first choice for most seniors. Does public housing have a negative image among seniors, and if so, what can be done about that? What role do PHAs want to play in this market, and how are they going to play it? How can they provide attractive, safe and supportive living environments? Where will the funding come from? Can some of the funding come from the Medicare/Medicaid streams?

Asset management can be a valuable tool when used within the framework of the social goals of the public housing program, but asset management is not the principal job of PHAs.

Supportive Housing for Very Low-Income Families with Children (the Unemployed and Underemployed)

There will always be some very low-income families with children, where the adult does not have a steady job, not even one with a low wage. This seems almost inevitable in our system for a variety of reasons. One is that it is the official policy of the Federal Reserve Bank to minimize inflation, and this can be done only by insuring that the job market never gets too tight, which in turn means that there will always be a large unemployed or underemployed group. The second is that our society does little to invest in education, job training or health care for those at the very bottom of our economic ladder. Some PHAs have said that they do not wish to serve as “housing as last resort” for the poorest of the poor, but all PHAs should set aside a significant proportion of their units for households in this group and arrange for supportive services.

People with Physical and Mental Disabilities, Including HIV/AIDS

PHAs can play a wide variety of creative roles in this area. This will almost always involve working with other agencies at the state and local level. In some cases, PHAs will be able to receive funding from other federal agencies such as the Department of Health and Human Services (HHS), either directly or indirectly.

It is sometimes claimed that the primary job of PHAs is “asset management.” HUD says it agrees. Many PHA directors agree. I respectfully disagree.

The term “asset management” in the real estate field means that property owners need to continually review the economics of their various properties, including the projected future income from each property, as well as the projected future costs associated with operating, maintaining and (where necessary) upgrading each property. Then they calculate what their expected rate of return is on various properties over some future time period, as well as what their rate of return might be if they developed new properties. Then property owners make decisions based upon how they can maximize the overall rate of return on their investments. If possible, they raise rents, keeping in mind that their properties must compete with other properties in the same market. They also decide what level of amenities is desirable, as well as how much money to spend on maintenance and modernization. If the calculation for an individual property seems to indicate a probable low future rate of return, they consider options such as selling the property, demolishing it, or converting it to other use. In all of these decisions, the goal is to maximize the return on investments.

PHAs also have property to manage, and of course they need to consider the physical and financial condition of individual properties as they decide whether it is worth making continued investments in each property. But, unlike the private sector, it is not a PHA’s principal goal to maximize the financial return on its housing properties over the long term. PHAs have social goals, and the principal one is to provide affordable housing to very low-income households. This social goal takes precedence over the goal of maximizing return on investment, which might be achieved, for example, by raising rents and/or seeking higher-income residents.

Most large organizations operate and maintain some type of physical plant. A school department operates and maintains many schools. No one, however, says that the principal goal of a school department is asset management. Its principal purpose is to educate. Its physical plant is one necessary tool for doing that.

A similar situation exists in the case of public housing, which like a public school system is an institution with a social purpose. Asset management can be a valuable tool when used within the framework of the social goals of the public housing program, but asset management is not the principal job of PHAs.

In my opinion, the principal objective of PHAs is to provide decent, safe and sanitary housing that is affordable to very low-income households so that they will have a sound base for their other activities of life (holding a job, going to school, etc.), have more money for other essentials such as food, health care and transportation, and be able to make some progress in improving their own economic condition.

The Role of the Private Sector

There are many ways in which PHAs can work with the private sector. PHAs can contract with the private sector for management services, maintenance, security, various other administrative tasks (e.g. payroll), insurance, resident training, resident services, and a variety of other activities. PHAs can also develop relationships with the private sector to help residents link up with jobs, job training and job referral services. There may be many other desirable forms of involvement, too.

The history of the HOPE VI program shows that it has been extremely difficult to secure private investment in these complex and risky deals. According to one GAO report, only 12 percent of the funds claimed as “expected to be leveraged” by PHAs in their HOPE VI plans is expected to come from the private sector. The inability to close these complex deals and get them approved by HUD has also been a major reason why HOPE VI has progressed so slowly, with fewer than 20 out of a total of over 165 HOPE VI revitalization grant awards having been completed as of HUD’s latest reports.

Recently, HUD has come up with something called the Public Housing Reinvestment Initiative (PHRI), under which PHAs would supposedly be able to borrow money in the private sector for their modernization and other capital improvements needs. HUD says this is intended to be a partial replacement for HOPE VI. Yet it appears that PHRI would depend heavily upon the availability of housing choice vouchers in the future, for use in these deals, and the future of Section 8 itself seems at best uncertain. (HUD is proposing block granting housing choice vouchers and turning them over to the states. HUD is also saying that it wants to reduce the average amount of each voucher.) PHAs have also come up with new ways of floating bonds on their own, asserting that they will have enough operating or capital funds to pay back the private sector.

I think that if Congress and HUD would provide multi-year budget authority and appropriations for these purposes, then it would be reasonable to seek private sector investment in public housing development, revitalization or other capital improvements. The risk to the private sector would be low, and the time and effort involved in creating these deals would be less. The costs to the PHAs and the public housing program would be less. However, this is not the case now.

For HUD to say that in the future PHAs must turn to the private sector for such investments also makes it seem as if there is an inevitable trend that the federal government will get out of the business of providing adequate funding for public housing operations, modernization, revitalization and replacement. I disagree. This is not inevitable. The federal government provides funding for a lot of things, and public housing is a better purpose than many. It should continue to provide such assistance to public housing.

HUD Is in Need of Major Overhaul

HUD is doing a terrible job of overseeing the nation’s public housing program. This cannot be allowed to continue.

What can explain why HUD itself has become such a disaster for the public housing program? I think one reason is the nearly total lack of interest at the top levels of HUD as to what HUD’s statutory mission is and what HUD is supposed to be doing. Many must never have read any of the statutes under which Congress has established the nation’s housing programs, or the Congressional intent behind them.

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Many top HUD officials appear to be oblivious to the fact that they are supposed to support the nation’s housing programs and help PHAs and other housing delivery systems provide affordable housing. Instead, they apparently consider their job to be:

- giving speeches saying that everyone should become a homeowner, regardless of their income or circumstances (this while mortgage default rates are rising);
- issuing ever-more-detailed and unreasonable report cards to PHAs; and,
- making excuses for why they have not asked and will not ask for adequate funding for the housing programs they are charged with administering.

Consider the following:

- The Allowable Expense Level (AEL), which HUD uses for the public housing operating subsidy eligibility calculation, was established in 1973. Whatever amount a PHA was spending (per unit) in 1973 became its PFS (Performance Funding System) base in 1975 (with the exception of a very small number of PHAs considered “above range” that were subsequently brought down “into range”). Since 1975, the AEL has been adjusted only by a modest inflation factor each year for 28 years. HUD has given no consideration to the changing operating circumstances of PHAs, the deterioration of the public housing stock due to inadequate capital funding, the changing population served, changing statutes and regulations that apply to public housing, the changing patterns of unionization, or the impact of costs (such as employee health benefits) that have increased faster than ordinary inflation.
- The only time that HUD has *ever* sent inspectors into the field to evaluate the modernization needs of public housing systematically and carefully was in 1985. A sample of over 900 public housing developments was inspected that year. A report was published in 1987 saying that in order to eliminate the backlog of modernization needs in 10 years, as well as keep up with new needs accruing as a result of normal aging and wear and tear, HUD should

request and Congress should appropriate over \$4 billion a year for public housing modernization. (HUD has never asked for such sums.) This study also identified about 80,000 units of public housing with “high end” needs, *i.e.* over \$40,000 per unit in modernization needs, but said it could not estimate, given the limited time available, what it might cost to redevelop or replace those units.

- In 1992, the National Commission on Severely Distressed Public Housing (NCSDPH) issued its Final Report. In it, the Commission said that it did not know how many units of severely distressed public housing there were, but it developed criteria for evaluating public housing developments to determine this, and urged HUD to do that as quickly as possible. Lacking any such information, it *estimated* that it would cost a little over \$7 billion to redevelop or replace the 80,000 units mentioned as having “high end” modernization needs in the 1985 survey. HUD has never conducted such an evaluation. No one to this day knows how many SDPH units or developments there were then or are now.
- In 1998, Congress passed a law reformulating public housing subsidies into the “operating fund” and the “capital fund,” and called upon HUD to establish new formulas and procedures for allocating each, based upon real needs. When the “operating fund” negotiated-rulemaking panel sat down to do its work, HUD brought no new information to the table about the costs of operating well-managed public housing. HUD had apparently not even considered that it might be HUD’s job to do this kind of research. When the capital fund negotiated rulemaking panel began getting ready to do its job, HUD hastily contracted for a consultant to gather some information from a few public housing developments as to what it would cost to “restore them to original condition.” (Since most public housing was built between 1937 and 1970, this meant that the HUD study was basically a survey of “repair” needs, not an evaluation of what was needed to truly modernize and upgrade various major building systems, such as electrical, plumbing, heating systems, etc., to current standards. It also did not include any estimate of the costs needed to improve the design and appearance of public housing so that it would be more attractive and blend better into the surrounding neighborhoods.) HUD then brought this information to the table and said this was a modernization needs study, which it definitely was not. The operating fund panel made a few tweaks to the formula, and called for further study. The capital fund study condemned the HUD study, but then agreed to let it be used to make a few tweaks to the capital formula.
- HUD has never responded to the call of the NCSDPH to use the Commission’s criteria to evaluate how many developments and units of severely distressed public housing there were then (or are now). Nevertheless, HUD announced in 2003 that the goals of the HOPE VI program had been accomplished because over 100,000 units

of public housing had been approved for demolition. Given the substantial underfunding of public housing operating and capital funds over the past decade, I personally believe that there are probably *more* severely distressed public housing developments today than there were 10 years ago.

- The recent study of public housing operating costs carried out by the Harvard Graduate School of Design used a methodology which had been examined in two major studies by Abt Associates, Inc., one in 1982 and one in 1993. In both of those studies, the consultant decided that there were major problems in comparing cost data from the HUD subsidized FHA-insured stock with data on the operating costs of public housing.
- HUD has rules and procedures concerning how utility costs will be funded. When actual utility prices, as paid by PHAs, exceed the predicted prices used for the initial determination of operating subsidy eligibility, PHAs are eligible for an end-of-the-year utility adjustment equal to 100 percent of the difference. HUD routinely requires that PHA do these calculations, but then ignores the increased subsidy eligibility, simply telling PHAs: It’s not going to happen, and don’t even think about asking for the money. As a result, PHA operations are underfunded to the tune of hundreds of millions of dollars every year. This is outrageous!
- HUD has repeatedly been unable to predict how much money it will need to renew Section 8 contracts plus or minus \$2 billion in any one year. This has frustrated Congress and resulted in the possibility that the program will be underfunded in the future.

Some of the things that HUD must do in order to fulfill its own legal responsibilities are:

- Make an estimate of the amount of funding that is needed every year in order that local agencies may carry out their missions successfully. *Make these estimates public and explain the details.*
- Ask the White House, OMB and Congress for adequate funding. Fight for adequate funding for the Department’s programs, like every other department does.
- Distribute the funding provided fairly, equitably, on a timely basis and in proportion to need.
- Monitor the expenditure of funds to ensure that such funds are spent legally and appropriately, and that accurate financial records are kept by local entities.
- Get its own record-keeping systems in order so that it knows how much money it is spending and for what.

OMB and the White House

No significant decisions about public housing or Section 8, or their funding levels, are made at HUD any more. Top HUD officials simply act on instructions from the White

House and OMB. In order to influence major decisions concerning public housing and Section 8, therefore, it is necessary for PHAs to go to the President, the Vice President, their chief domestic policy advisors and OMB.

OMB is always looking for ways to cut funding for public housing and Section 8. Then OMB tells HUD what kinds of budgets to submit every year. Then OMB cuts them further. There is no commitment on OMB's part to provide funding levels that are adequate to operate, maintain and modernize public housing, much less to replace the developments when they reach the end of their useful life span.

OMB's agenda for a long time, including during the Clinton Administration, has been to gradually get rid of family public housing, because OMB claims that all project-based subsidy programs cost more than vouchers. But that is not the end of OMB's agenda. For over a decade, OMB has claimed that it would be desirable to convert all project-based housing subsidies to tenant-based assistance, block grant it and turn it over to the states, and then merge it with the welfare program (and its successor TANF), effectively eliminating a separate program of housing assistance entirely.

I suspect that in order to get at the folks at OMB, you have to get the attention of the senior domestic policy staff in the White House. That means the President will have to OK these ideas. The next presidential election is in 2004 and the primaries are coming up in a few months. The candidates are starting to put together their teams and their platforms now. Get to them and demand that housing be on the agenda, that PHAs and public housing be on the agenda, and that the federal government support housing programs and get some people in at the top levels of HUD who are committed to this.

Improving Existing Funding Mechanisms

This section sketches out some very quick ideas about modifying existing funding systems for public housing, *i.e.* the public housing operating and capital funds.

PFS has been in place for 30 years, and has never been changed substantially, largely because no one has been able to come up with adequate proof that an alternative would be better or more equitable. Lacking convincing arguments, any discussion of possible changes quickly deteriorates into a "formula war," *i.e.* a brawl about dividing up the existing pie in some new way. It will only be possible to make significant improvements in the system if there is more money.

I think that the goal of creating some new formula for the operating fund that will then be locked into place for the next 30 years, as PFS was, is a mistake. Probably the worst thing about PFS is that it is so rigid, and so unable to respond to changing circumstances and needs. Why repeat this for the next 30 years, using a slightly different formula?

Just going back to a negotiated rule-making process that has the mandate of taking the results of the Harvard study and converting them into a new formula is pointless. This wouldn't get at the principal issue, which is how much does it cost to run well-managed public housing—the question the Harvard study was supposed to answer but didn't.

I think it is reasonable to say that public housing should

cost *no less than* a housing choice voucher on a per-unit basis. The most important goal is to get the total public housing figure increased substantially, *e.g.* to around a total of \$8 billion.

I think that another major change that is needed to accompany this is to establish a Board of Adjustment that would annually hear a limited number of appeals, and make adjustments of housing authorities' Allowable Expense Level (AEL). The mandate of the Board would be to select from among all of the appeals submitted to it those that seemed furthest out of line, and limit its efforts each year to those. Gradually over time it could eliminate the worst disparities. The Board of Adjustment would need to comprise true housing professionals appointed from outside of HUD. They would make recommendations to HUD, and the HUD Secretary would have the final say.

The total amount of the subsidy to public housing should include amounts that would enable PHAs to replace their developments when they have reached the end of their useful lifespan. The amount should also be adequate to enable PHAs to manage their stocks according to all applicable statutes and regulations. These require PHAs to do things that private housing managers do not have to do.

What are the adequate costs? I do not think that it is possible to develop one absolute standard for all public housing. But one could develop estimates of what it would cost to provide different levels of services under different operating conditions and circumstances, and then Congress can make a choice about what level it wants to fund. For example, you could say that *if* you wanted to provide one full-time social worker for each 80 individuals living in senior public housing, it would cost so much per year.

I also think that public housing subsidies should be increased to include a much larger element of Payment in Lieu of Taxes (PILOT). Public housing now is often rejected because local communities believe it costs far more to the local community than the PHAs provide in the way of PILOT. PHAs need to receive from the federal government enough money to fully cover the costs to the local community, and more than pay their own way (*e.g.* in terms of costs of local services, schools, etc.) and *also* provide an incentive to the local community. Trying to keep PILOT low will result in increased competition to get out of the low-income housing business by local communities. HUD needs to provide local communities with a substantial incentive to accept such housing, by covering its direct costs and then some.

The most important thing that could be done with the capital fund is to get it up to where it should be, *i.e.* around \$4 billion a year.

Conclusion

Political and social conditions can change. I hope that in the not-too-distant future our nation will realize that in order to survive as a society, we need to acknowledge that we are all in the same boat, rich and poor, and need to pay attention to the needs of all Americans, not just the top 10 percent. There once was a day when Americans were glad to help each other build their houses. Maybe that day will come again. ■