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Subcommittee on Housing and Community Opportunity

United States House of Representatives



“The Impacts of Late Housing Assistance Payments on Tenants and Owners
in the Project-Based Rental Assistance Program”

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Chairwoman Waters, Ranking Member Capito, and other distinguished Subcommittee Members, thank you for the opportunity to appear before you today to address concerns raised over HUD's ability to fund and pay the annual renewals of Section 8 project-based housing assistance payment (HAP) contracts with funding available in Fiscal Year (FY) 2007 and requested for FY 2008. In my testimony today, I will: (1) reassure you that this Administration's policy remains in support of fully funding all HAP contract renewals as a needed source of affordable rental housing for nearly 1.25 million low-income families; (2) explain the program funding and payment issues experienced in FY 2007 and the Department's solution for resolving those issues; and (3) address the funding needs in FY 2008 to fully support this important housing program.

Background

HUD's Section 8 project-based housing assistance program serves to maintain the supply of affordable rental housing units for nearly 1.25 million low-income households. Under this program, either directly or through contract administrators, HUD makes housing assistance payments to private owners of multifamily housing. These payments help make project-based housing and related utilities affordable for lower income households. Under HUD's HAP contracts with these private owners, low-income tenants generally pay 30 percent of their adjusted income toward their rent, with the monthly HUD subsidy payment equal to the difference between what the tenants pay and the contract rents that HUD and the owners negotiate in advance. As an incentive to spur the private development of low-income housing in the late-1970s and early-1980s, Congress appropriated funding to enable HUD to execute long-term, typically 20- to 40-year HAP contracts. The varying tenant income levels and contract rent adjustment factors make it difficult to estimate HAP contract funding needs from year to year, let alone over a long term. As a result, the funding requirements for many of the long-term contracts executed in the 1970s and 1980s were either underestimated or overestimated. HUD has dealt with this issue by recapturing excess funds from long-term contracts as they expire and using those funds to provide additional funds to the contracts that were under-funded through contract amendments. Generally, HUD has recaptured significantly more from the expiring contracts than has been needed to cover the cost of the amendments. That excess, along with any excess funding found in other HUD programs is proposed for rescission each year.

As the initial 20- to 40-year HAP contracts began to expire during the 1990s, each successive Congress and Administration has sought legislative authority to renew the HAP contracts to preserve this important source of low-income housing. This goal led to the enactment of the Multifamily Assisted Housing Reform and Affordability Act of 1997 (MAHRA), enacted on October 27 of that year. In MAHRA, Congress eschewed the original Section 8 approach of appropriating funding in an amount sufficient to provide payments for a 20-, 30-, or 40 year term and instead permitted the Department, in most cases, to renew the contract for a term committed to the sound discretion of the Department. In all cases, however, the Department's duty under MAHRA to fund a

renewal contract for any given year, regardless of the contract term, is explicitly subject to the condition that Congress makes sufficient amounts of funding available each year in the Department's appropriation Acts. In general, HUD reduced the terms of the subsequent renewals to 1- or 5-year terms, with funding renewed annually, subject to appropriations. Contract renewals with terms of greater than one year included language noting that they, too, are "subject to annual appropriations," meaning that the terms apply only if HUD gets future appropriations sufficient to fund the contracts for each annual period beyond the first year. HUD currently administers over 18,000 HAP contracts to provide about 1.25 million low-income housing units. Of these contracts, 12,910 contracts, covering over 915,000 housing units, are subject to annual funding renewals.

As budgets became even tighter after 1997 and in this decade, HUD was often forced to partially fund some annual contract renewal terms for fewer than 12 months. HUD would fully obligate funding for as many monthly contract payments as financially feasible and wait for additional funding in the following federal fiscal year to complete the 12-month funding. This partial or "incremental" funding practice became more frequent in recent years. In the event that current appropriations and recaptured funding is insufficient to both renew all HAP contracts for a full 12-month term and to meet the Department's rescission mandate for the current fiscal year, the practice can shift some funding needs to the next fiscal year.

FY 2007 Funding and Current Payment Issues

While HUD thought its partial funding practice was acceptable – because the contract terms referenced funding as "subject to the availability of sufficient appropriations" – a closer review of the actual contract language and program funds control processes revealed that the intended "incremental funding" practice was not adequately captured in the wording of the contracts. In particular, the statement that the contract would run from year to year "subject to the availability of sufficient appropriations to make housing assistance payments for any year," did not make it clear that HUD might be obligating less than 12 months of funding at the time each renewal contract was executed. HUD did not have sufficient funding available to both fully fund all FY 2007 contract renewals for a 12-month period and meet HUD's \$1.65 billion rescission mandate for FY 2007. At the time HUD discovered this problem, all but 1,728 of the 12,910 annual contract renewals had already been executed with 12-months of obligated funding, exceeding the funding HUD had originally planned to obligate for those contracts in FY 2007.

HUD developed and executed the following strategy to remedy the situation without terminating any contractual relationships or necessitating additional appropriations late in the fiscal year and in a constrained budget environment:

1. First, HUD fully obligated 12 months of funding on contract renewals that had already been executed in FY 2007 under previous contract terms. (See example of old contract terms in Attachment 1.)

2. Secondly, HUD revised key language in the renewal contract forms for the 1,728 contract renewals remaining to be processed in FY 2007, and for future renewals, to correctly implement an “incremental funding” clause to enable HUD to properly split the funding of annual contract renewals between two consecutive federal fiscal year appropriations. (See example of new contract terms in Attachment 2.)
3. Lastly, HUD re-estimated the funding needs of the remaining “long-term” Section 8 contracts and recaptured all excess funds for use in covering HUD’s FY 2007 Section 8 contract renewal funding needs and rescission mandate.

HUD has successfully executed this strategy to provide funding for the renewal of all HAP contracts into FY 2008 and avoid the need for additional appropriations or the unintended rescission of unobligated funds in other HUD programs. Regrettably, many of our business partners experienced contract payment delays as we developed and executed this strategy. While we took steps to provide as much relief as possible – such as allowing owners to borrow against project reserves or requesting mortgage forbearance – many FY 2007 payments were not paid on time. I realize that some of our housing program partners may have experienced hardships during this transition period and I apologize on behalf of the Department.

HUD’s current contract renewal and payment process involves multiple manual steps and participants and averages four weeks to complete negotiations and fully execute the contract to enable payment. HUD’s funds control practices and accounting systems require that an active executed contract be in place with sufficient obligated funding to cover the specified contract term before any payments can be released for that contract. An owner cannot receive a monthly payment on a contract that HUD and the owner have not properly renewed. HUD sent the 1,728 fourth-quarter FY 2007 revised contract renewal packages, including the revised contract forms, to the contract administrators for processing the first week in September 2007, and all but 428 of the contracts were negotiated, executed and entered into HUD’s system to facilitate payment by the end of September. As of last week, fewer than 250 FY 2007 contract renewals remained to be executed by owners and the number declines daily.

Contract renewals due in October of each year – the first month of the federal fiscal year – normally experience a one-month payment delay because the new fiscal year appropriation is not available until the same day payment is due to the owners – on October 1st – and it generally takes HUD two to three weeks to transition its books and financial systems from one fiscal year to the next. November renewals often experience payment delays in the first month, too. The simplest resolution to these delays is to begin processing both October and November contract renewals earlier, in August and September, with respective effective dates and final funding actions on October 1st and November 1st. HUD needs to alter its processing of October and November renewals to avoid payment delays next year and beyond.

Program Funding Needs for FY 2008

In resolving the FY 2007 HAP contract funding issues, HUD has performed considerable additional analysis on its budget needs for FY 2008. The President's FY 2008 Budget – which was submitted in February 2007 before HUD's FY 2007 program funding issues were identified and resolved – requested \$5.522 billion for Section 8 HAP contract renewals and proposed a \$1.3 billion rescission that was primarily intended to come from excess Section 8 Program funding. HUD's current analysis indicates it can meet the FY 2008 HAP contract renewal funding needs with the funding level in the President's FY 2008 Budget, and HUD estimates it can meet the rescission target with Section 8 and other HUD program resources.

Given that many HAP contracts were forward funded into FY 2008 with available FY 2007 funds, and with continued use of the new incremental funding clause for the FY 2008 contract renewals, HUD would require, and the President's Budget supports, a FY 2008 program funding level of \$5.6 billion to incrementally fund all FY 2008 contract renewals through November of 2008. Incrementally funding the FY 2008 contract renewals two months into FY 2009 will allow sufficient time to process another round of incremental funding actions at the beginning of the next new fiscal year to avoid further late payment problems for housing owners; that is, if Congress enacts HUD's FY 2009 appropriation bill in a timely manner.

Conclusion

HUD is committed to continuing to improve its systematic means to more accurately forecast budgetary needs so that each year's budget request is sufficient to fund all annual Section 8 HAP contract renewals, as well as any amendment needs on remaining long-term contracts. We are in the process of concluding a contract-by-contract data clean-up in our program data system as a first step in reengineering the long-term solution to streamline and automate the overall Section 8 Project-Based Assistance Program budgeting and contract management and payment processes. Implementation of the necessary systems changes is subject to the availability of sufficient information technology systems funding for HUD's Working Capital Fund. The Department is committed to supporting HAP contract renewals to assist both the property owners and the families they serve. We will continue to work with our business partners and the Congress to improve the administration of this critically needed housing program.

That concludes my prepared testimony and I stand ready to address your questions. Thank you.

**HUD's Old Annual Funding Terms
For Section 8 Project-Based Assistance Contracts**

2 TERM AND FUNDING OF RENEWAL CONTRACT

- a** The term of the Renewal Contract begins on
_____.
- b** Subject to the availability of sufficient appropriations to make housing assistance payments for any year in accordance with the Renewal Contract, as determined by HUD, the Renewal Contract shall run for a period of five (5) years, beginning on the first day of the term. Section 8 housing assistance payments to the Owner during the Renewal Contract shall only be made from budget authority appropriated by the Congress, and available for this purpose.

**HUD's New Incremental Funding Terms
For Section 8 Project-Based Assistance Contracts**

2 TERM AND FUNDING OF RENEWAL CONTRACT

- a** The Renewal Contract begins on _____ⁱ
and shall run for a period of one year.
- b** Execution of the Renewal Contract by the Contract Administrator is an obligation by HUD of \$ _____,ⁱⁱ
an amount sufficient to provide housing assistance payments for approximately _____ⁱⁱⁱ months of the Renewal Contract term.
- c** HUD will provide additional funding for the remainder of the Renewal Contract term subject to the availability of sufficient appropriations. When such appropriations are available, HUD will obligate additional funding and provide the Owner written notification of (i) the amount of such additional funding, and (ii) the approximate period of time within the Renewal Contract term to which it will be applied.

ⁱ The Renewal Contract must be entered before expiration of the Expiring Contract. Enter the date of the first day after expiration of the term of the Expiring Contract.

ⁱⁱ Enter the amount of funding obligated.

ⁱⁱⁱ Enter a whole number of months.