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Report to the Congress; by Elmer B. Staats, Comptroller General.

Issue Area: Domestic Housing and Community Development: Minimizing Mortgage Insurance Losses (2108).
Contact: Community and Economic Development Div.
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Organization Concerned: Department of Housing and Urban Development.
Congressional Relevance: House Committee on Banking, Currency and Housing; Senate Committee on Banking, Housing and Urban Affairs; Congress.
Authority: National Housing Act of 1934, as amended (12 U.S.C. 1701). Housing and Urban Development Act of 1968.

The Department of Housing and Urban Development (HUD) began insuring multifamily housing projects in 1938 and, in 1954, began implementing subsidized multifamily housing programs to enable low- and moderate-income families to improve their housing conditions. Findings/Conclusions: Recently HUD has incurred many financial losses due to mortgage defaults, foreclosures, and assignments on its multifamily loan insurance programs. Among the problems causing failures were that the underwriters frequently overestimated revenues, underestimated expenses, and did not have supporting documentation. Actual annual revenues for 13 of 30 projects examined were from 1% to 46% less than HUD estimates, and actual annual expenses for 27 of the projects exceeded estimates by from 5% to 110%. HUD's major effort to improve its underwriting process through computerized information on the incomes and expenses of operating multifamily projects was inaccurate, incomplete, and outdated. Contrary to HUD procedures, underwriters at times used property assessment methods and tax rates not applicable to the areas where proposed projects would be located, resulting in unrealistically low estimates of property tax costs. Accurate estimates would help in identifying alternatives to improve financial viability, but once a project is approved, essentially the only options available are to increase rents and/or provide a moratorium on the interest and principal payments for a short-term period. Recommendations: The Secretary of HUD should: insist that field offices maintain accurate, complete, and up-to-date information in the computer base used to evaluate proposed projects; insist on underwriters' strict adherence to procedures for preparing real estate tax estimates; require that uniform methodologies be devised and used in projecting the impact of inflationary trends; clarify procedures regarding estimating occupancy levels; examine the possibility of

establishing a safety margin which would increase cash flow to cover contingencies during the first few years of project operation; and reemphasize the importance of the underwriting function in objectively and accurately evaluating elements of mortgage risk. (Author/HTW)

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BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

HUD Needs To Better Assess Financial Soundness Of Multifamily Residential Projects Before Insuring Them

The Department of Housing and Urban Development has inadequately assessed the financial soundness of multifamily residential projects before insuring them. Project operating results were not as favorable as anticipated during project approval.

Under such circumstances the Department unknowingly approved financially unsound projects and projects for which the risks of default were higher than anticipated. This situation contributed to the $263 million loss the Department experienced on the multifamily properties acquired and sold since fiscal year 1972.

The Department's financial risks can be reduced before these properties are insured. GAO recommends several improvements for estimating multifamily project revenue and expenses to better assess the financial soundness of such projects.

UNITED STATES GENERAL ACCOUNTING OFFICE

CED-78-70

MARCH 29, 1978

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-114860

To the President of the Senate and the
Speaker of the House of Representatives

This report examines the practices for assessing the financial soundness of multifamily projects insured by the Department of Housing and Urban Development. The report addresses the problems experienced in underwriting multifamily projects and points out the need for improvements to reduce the Government's risk in insuring them.

We made our review pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Accounting and Auditing Act of 1950 (31 U.S.C. 67)

We are sending copies of this report to the Acting Director, Office of Management and Budget, and to the Secretary of Housing and Urban Development.

Elmer B. Staats

Comptroller General
of the United States

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

HUD NEEDS TO BETTER ASSESS FINANCIAL SOUNDNESS OF MULTI-FAMILY RESIDENTIAL PROJECTS BEFORE INSURING THEM

D I G E S T

Recently the Department of Housing and Urban Development incurred a string of financial losses due to mortgage defaults, foreclosures, and assignments on its multifamily loan insurance programs.

Among the problems causing the failures were that underwriters

--frequently overestimated revenues,
--underestimated expenses, and
--did not have supporting documentation.

Actual annual revenues for 13 of 30 projects GAO tested were 1 to 46 percent, or $3,000 to $253,000 less than Department estimates.

Actual annual expenses for 27 of the 30 projects exceeded Department estimates by 5 to 110 percent, or $4,000 to $225,000. (See p. 8.)

GAO recognizes that underwriting is not a precise science. Many factors must be evaluated and the accuracy of estimates can be affected by such unpredictable events as strikes and rapid changes in the economy.

However, correcting weaknesses will result in more accurate underwriting estimates and better assessments of the financial soundness of proposed projects.

The Department's major effort to improve its underwriting process through computerized information on the incomes and expenses of operating multifamily projects was inaccurate, incomplete, and outdated.

Information in the Department's computer files at one location was inaccurate by 12 percent for the number of apartments, 29 percent for room dimensions, and 15 percent for locations. The

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computer information on file at another site was so inaccurate it was purged from the system, and steps were initiated to obtain better information for use in evaluating proposed projects. (See p. 21.)

Also, contrary to Department procedures, underwriters at times used property assessment methods and tax rates not applicable to the areas where proposed projects would be located. Project expense estimates contained unrealistically low property tax costs as a result. (See p. 25.)

Accurate estimates of operating results afford an earlier opportunity to identify alternatives for improving the financial viability of higher risk proposals. Once a project is approved for mortgage insurance, the Department's options are reduced essentially to increasing rents and/or providing a moratorium on the interest and principal payments for a short-term period.

On the other hand, before the mortgage is approved, HUD can require that the project scope be revised, the sponsor can put more money into the project, an escrow account can be established for future contingencies, or the proposal can be rejected.

RECOMMENDATIONS

GAO recommends that the Secretary of Housing and Urban Development, to better assess the financial soundness of multifamily projects proposed for insurance:

--Insist that field offices maintain accurate, complete, and up-to-date financial and project characteristic information in the computer base used to evaluate proposed projects, including assigning adequate staff with proper training to implement underwriting objectives.

--Insist on underwriters' strict adherence to underwriting procedures for preparing real estate tax estimates, aggressively seeking information on utility costs, and maintaining documentation to support estimates of project revenues and expenses.

--Require that uniform methodologies be devised and used in projecting the impact of inflationary trends on proposed projects.

--Clarify procedures regarding estimating occupancy levels.

--Examine the possibility of establishing a safety margin which would increase cash flow to cover contingencies during the first few years after a project becomes operational.

--Reemphasize the importance of the underwriting function in objectively and accurately evaluating elements of mortgage risk.

AGENCY COMMENTS

The Assistant Secretary for Housing agreed with GAO's recommendations and outlined corrective actions underway or planned. (See p. 39.)

C O N T E N T S

ABBREVIATIONS

CMHIF	Cooperative Management Housing Insurance Fund
FHA	Federal Housing Administration
GAO	General Accounting Office
GIF	General Insurance Fund
HUD	Department of Housing and Urban Development
OIG	Office of Inspector General
MMIF	Mutual Mortgage Insurance Fund
SRIF	Special Risk Insurance Fund

CHAPTER 1

INTRODUCTION

By enacting the Housing and Urban Development Act of 1968, the Congress reaffirmed the Nation's housing goal of a decent home and suitable living environment for every American family. Between 1969-78, 26 million housing units would be constructed or rehabilitated--6 million for low-income families.

The Department of Housing and Urban Development (HUD) through its Federal Housing Administration (FHA) administers unsubsidized and subsidized multifamily mortgage insurance and loan programs. FHA's principal purposes are to (1) improve home-financing practices, (2) act as a stabilizing influence in the mortgage field, (3) encourage improvements in housing standards and conditions, and (4) prevent the deterioration of residential properties.

The National Housing Act, as amended (12 U.S.C. 1701 et seq.), allows HUD to insure mortgage loans made by private lending institutions on various types of housing, including multifamily rental housing projects. Parties to a multifamily mortgage insurance transaction are the mortgagee (the lender), the mortgagor (the projectowner), and HUD.

HUD began insuring multifamily housing projects in 1938, when it implemented section 207 of the National Housing Act of 1934, as amended (12 U.S.C. 1713), which was designed to improve the housing conditions for millions of moderate-income families by insuring unsubsidized mortgage loans. In 1954 HUD began implementing subsidized multifamily housing programs to enable low- and moderate-income families to improve their housing conditions.

MULTIFAMILY MORTGAGE INSURANCE WRITTEN AND IN FORCE

From its inception in 1934 to February 28, 1977, HUD insured mortgage loans amounting to about $184 billion; about $104 billion was in force in 1977. About $34 billion of the $184 billion represents written multifamily mortgage insurance, of which about $21 billion was in force at February 28, 1977. About 26,170 multifamily properties, representing 2,569,059 housing units, have been insured by FHA.

These figures reflect the activities of 32 multifamily programs, 10 now expired, administered by HUD. Four major HUD multifamily housing programs reviewed are included as appendix II.

The following chart shows that HUD expects to play a major role in promoting the development of multifamily projects in the near future.

Insurance written	Estimated number of multifamily units
1976	63,127
Transition quarter	25,750
1977	98,564
1978	171,609

MULTIFAMILY MORTGAGE LOSSES

During the past several years, HUD has experienced a large number of multifamily insurance claims and considerable losses on the multifamily properties it sold.

If an insured mortgagor defaults, the mortgagee may acquire the deed through foreclosure and convey the title directly to HUD for full insurance benefits or may assign the mortgage directly to HUD and forfeit 1 percent of the unpaid principal. The lengthy and expensive foreclosure process in most States influences a mortgagee to assign the mortgage to HUD.

HUD incurs losses when the cost to acquire and hold properties in inventory exceeds the price obtained when the property is sold. From fiscal year 1972 to February 28, 1977, HUD nationally lost $263.4 million on 555 multifamily properties sold, for an average return of only 58 cents on each dollar invested. As of February 28, 1977, HUD's inventory of multifamily properties and loans totaled 2,092, representing 256,528 housing units acquired at a cost of about $3.2 billion.

The following table details HUD's sale of multifamily project during 1972-77.

Percentage of Investment Returned on HUD Multifamily Properties Sold During 1972-77

FY	Number of properties sold	Sale price	HUD investment cost	Return on HUD investment (percent)
		-----(millions)-----		
1972	22	$ 26.1	$ 25.1	104
1973	72	81.2	99.2	82
1974	81	56.4	104.7	54
1975	123	61.6	120.7	51
1976	152	81.4	156.6	52
TQ (note a)	47	24.6	43.0	57
1977 (note b)	58	31.5	76.9	41
Total	555	$362.8	$626.2	58

a/Transition quarter 1976--from July 1, 1976, through September 30, 1976.

b/As of February 28, 1977.

Because of the large number of defaults and foreclosures on multifamily properties, HUD implemented in February 1975 a moratorium on foreclosures of subsidized multifamily projects, which was lifted in January 1977. Hence, it is likely that many of the 2,092 multifamily properties and loans presently owned by HUD may end in foreclosure and sale with high losses to the Government.

IMPACT OF MORTGAGE LOSSES ON INSURANCE FUNDS

HUD's losses on multifamily projects have contributed to the approximately $3.2 billion combined deficit as of September 30, 1976, of three of four of its funds--the General, Cooperative Management Housing, and Special Risk Insurance. Of the $3.2 billion combined deficit, $1.5 billion is attributed to multifamily properties. The following table shows the reserve balance of HUD's four insurance funds by type of property as of September 30, 1976:

Insurance fund	Total reserves or deficiency(-)	Small homes deficiency(-)	Multifamily properties deficiency(-)	Property improvement loans
	(millions)			
Mutual Mortgage Insurance	$1,986.2	$1,986.2	$ -	$ -
General Insurance	-1,704.1	-786.9	-1,030.4	113.2
Cooperative Management Housing Insurance	21.8	-	21.8	-
Special Risk Insurance	-1,468.9	-972.0	-496.9	-
Subtotal	-$3,151.2	-$1,758.9	-$1,505.5	$113.2
Total	-$1,165.0	$ 227.3	-$1,505.5	$113.2

The insurance funds are described in appendix III.

For the first time, HUD's four insurance reserve funds had a deficit of about $183 million in June 1975. There was about a $1 billion increase during the 15 month period ending September 30, 1976, in the combined deficit ($1.2 billion) of the four insurance funds. Multifamily project losses during the same period increased $703 million.

HUD has financed the deficit in large part by borrowing from the Treasury. Outstanding borrowings have resulted in increasing interest costs to the funds, which have further drained available funds. In fiscal year 1976 the General Insurance and Special Risk Insurance Funds paid a total interest of about $389 million. Interest costs through fiscal year 1976 totaled about $813 million.

The 1976 Supplemental Appropriations Act provided $142.5 million to HUD to reimburse the Special Risk Insurance and the General Insurance Funds for partial losses incurred through June 30, 1975. Under the 1977 Appropriations Act, an additional $135 million was provided to further reimburse these two funds for losses. HUD requested an additional $1.8 billion in its 1977 supplemental appropriation request to cover losses in the two funds. Included in this amount is $15 million for reimbursement to FHA for losses incurred under the urban homesteading program.

UNDERWRITING--WHAT IT MEANS

The National Housing Act requires that projects approved for mortgage insurance be economically sound. The project is to offer an acceptable degree of risk, giving consideration to the needs of low- and moderate-income families. HUD's underwriting process is a key element in determining whether a multifamily project has a reasonable chance of success. If a project is approved without full knowledge of the risks involved, the risks assumed by the Government may be greater than anticipated and losses may be incurred by the insurance funds. HUD's underwriting for multifamily projects affords the Government an early opportunity to revise proposed projects to enhance the probability of approving financially viable projects.

The underwriting process involves the loan applicant submitting information which indicates his credit worthiness, construction cost estimates, revenue and expense projections, and other data. HUD procedures require that the proposal be evaluated as follows:

--A cost unit examines the reasonableness of proposed construction costs.

--An architectural and engineering unit determines the acceptability of physical improvements.

--A mortgage credit unit determines the (1) acceptability of the applicant's financial ability to complete the project and (2) adequacy of rental income to meet all costs and provide a reasonable return on invested capital.

--A valuation unit (referred to as the underwriting function in this report) analyzes the market need, location, earning capacity, expenses, taxes, and other costs of the property.

--HUD underwriters are required to test the accuracy of the applicant's projections by making independent tests of the information submitted and preparing their own estimates of construction costs and operating income. Such estimates are to be based primarily on data from similar projects. In addition, market supply, demand, and vacancies are evaluated. The result, therefore, is the product of an interdisciplinary team.

SCOPE OF REVIEW

We made our review at HUD headquarters, Washington, D.C., and HUD's Chicago, Detroit, and San Francisco area offices. We reviewed the provisions of the National Housing Act and examined the policies and procedures the area offices followed in performing multifamily underwriting activities relating to analyzing market need, location, earning capacity, and expense data. Sections 207, 220, 221, and 236 programs were selected for review because they represent the bulk of HUD's multifamily mortgage activities.

We selected 30 projects to compare actual operating results to those anticipated in project approval. These projects were selected to obtain representative coverage of the four HUD insurance programs for multifamily projects in the Chicago, San Francisco, and Detroit area offices. Projects were selected on the basis that HUD had made firm loan commitments between July 1, 1972, and June 30, 1976, and that the projects had been in operation for at least 1 full year. Also, we selected 16 additional projects for which underwriting had just been completed to evaluate HUD's multifamily underwriting process.

We interviewed HUD officials in the Chicago, San Francisco, and Detroit area offices, as well as city officials; private real estate, utility, insurance, and mortgage insurance firms; and commercial banks. We did not examine other facets of underwriting relating to reasonableness of construction cost estimates, architectural and engineering design, and mortgage credit activities.

CHAPTER 2

PROBLEMS EXPERIENCED IN UNDERWRITING MULTIFAMILY PROJECTS

HUD underwriters have inadequately estimated revenues and expenses for multifamily projects before insuring them. Generally, operating results were not as favorable as anticipated during project approval, and as a result, HUD assumed greater financial risks than anticipated. Inaccurate estimates of revenues and expenses also contributed to multifamily insurance program losses.

Accurate estimates of project incomes and expenses reduce the risk of default by enabling HUD management to make more informed decisions on whether to insure the loans. HUD is also afforded an earlier opportunity to identify ways to improve the financial viability of higher risk proposals, such as requiring the borrower to place money into escrow to cover predicted initial operating deficits.

Frequently, HUD underwriters overestimated revenues and underestimated expenses. Consequently, profits for some projects were smaller than anticipated, and for other projects, losses were actually sustained. Under such circumstances HUD has unknowingly approved financially unsound projects or projects for which the risks of default were higher than anticipated.

In addition, documentation to support the underwriters' estimates was often missing; therefore, little assurance exists that the estimates were properly prepared, and adequate supervisory reviews cannot be made of the underwriting process.

Twenty-one of the 30 projects reviewed had been in serious financial difficulty as of July 1977. Nine of the 21 projects had experienced default, and the mortgages of 8 have been assigned to HUD. The remaining nine properties have generated sufficient revenues to meet operating expenses and debt service payments. However, most of these projects increased rents or achieved higher than expected occupancy rates.

Some of the problems discussed in this report were identified by HUD's Office of Inspector General (OIG) in 1972 and again in 1975. However, no aggressive action has been taken to correct shortcomings in the multifamily underwriting process.

In August 1977 HUD's Task Force on Multifamily Property Utilization reported on the major problems faced by subsidized multifamily projects. The task force was established because of the financial difficulties many subsidized multifamily projects are experiencing. One major conclusion of the report was that multifamily project income was generally inadequate to cover project operating expenses. The report pointed out that for most projects the income problem was due, in part, to the initial overestimation of project income and the underestimation of project expenses during underwriting. In October 1977 HUD's Assistant Secretary for Housing testified before the Senate Banking, Housing and Urban Affairs Committee on the troubled state of multifamily projects and indicated that solutions to these problems will be presented to the Congress for consideration in early 1978.

This chapter explains the nature of the problems experienced by HUD underwriters for the projects we reviewed. Chapter 3 discusses steps that HUD can take to increase the accuracy and reliability of such estimates and, thereby, reduce the degree of risk associated with insuring costly multifamily projects.

UNREALISTIC PROFIT PROJECTIONS CAUSED BY OVERESTIMATING REVENUE AND UNDERESTIMATING EXPENSES

Estimating a proposed project's income and expenses is not a precise science. Many factors such as location, marketability, rental rates, occupancy rates, inflation, trending factors, and operating expenses, must be evaluated.

To determine how well HUD underwriters were performing, we selected 30 multifamily projects--10 each in Chicago, Detroit, and San Francisco--in operation for more than 1 year but not more than 2 years. We compared HUD estimates used for approving the projects with actual project operating data. Briefly, we found that:

--Actual annual revenues for 13 of the 30 projects were 1 to 46 percent, or $3,000 to $253,000, less than HUD estimates. For 8 of the 13 projects, HUD revenue estimates exceeded actual revenues by 7 or more percent.

--Expenses actually incurred annually for 27 of the 30 projects exceeded HUD-estimated expenses by 5 to 110 percent or $4,000 to $225,000.

Some of the dollar amounts of individual income and expense variances appear small when discussed separately by project. However, when all variances on a project are combined, they can indicate serious cash flow problems because many HUD estimates were approved with little margin for error. This is particularly true when a project encounters overestimated revenues and underestimated expenses.

Revenue estimates often too high

As shown in the following table annual revenues for 13 of 30 projects were overestimated from 1 to 46 percent, or $3,000 to $253,000. Revenues for the remaining 17 properties were underestimated from 0.1 to 16 percent, or $56 to $162,000.

Project revenues basically involve two factors--occupancy and rental rates. The underwriter usually assesses these factors by analyzing the demand for the proposed apartment complex in the area and rents charged for similar properties.

Extent to which revenues were overestimated annually

Percent	Less than $10,000	$10,001 to $50,000	$50,001 to $100,000	Over $100,000
1 to 5	3	2	-	-
6 to 15	1	4	1	-
16 to 30	-	1	-	-
46 and over	-	-	-	1
Total	4	7	1	1

Revenues were overstated because of errors in projecting occupancy rates for eight projects, rental rates for one project, and a combination of errors in predicting occupancy and rental rates for three other projects. For the remaining project, income from space available for business purposes was less than HUD estimated.

The following table shows the impact of overestimating revenues due to variances in occupancy and rental rates for the 12 projects that experienced these problems.

Project	Percent of occupancy HUD estimate	Actual	Average monthly rent HUD estimate	Actual	Revenue overestimated by Amount	Percent
Chicago						
A	93	80	$201	$207	$ 45,682	9
B	95	52	225	226	253,350	46
C	95	91	170	168	13,511	5
D	95	95	190	176	21,458	4
E	95	81	174	174	62,052	14
Detroit						
A	60	48	168	168	19,919	20
B	93	90	218	213	7,808	1
C	93	88	199	207	4,797	1
D	93	84	180	180	23,005	8
San Francisco						
A	93	92	194	181	16,801	7
B	93	85	278	290	2,509	2
C	95	84	148	150	16,966	11

As illustrated by Chicago's project A, failure to achieve the estimated occupancy rate can seriously reduce revenues ($45,682 annually, or 9 percent of estimated revenues), even though the actual average rent realized exceeded estimated rents by $6 a month.

The following examples describe the impact that overestimated revenues can have on a project's financial ability.

Project A

HUD insured a $3.6 million loan for this 216-unit section 221(d)(4) project (nonsubsidized) in October 1972. The underwriter originally estimated that the project would achieve a 93-percent long-term occupancy rate. However, because newer rental projects in the area were slower than normal in renting, the underwriter estimated first-year occupancy would reach only 50 percent. As a result it was determined that the loan applicant should be required to place $170,000 into escrow to cover this initial operating deficit. The loan applicant subsequently asked HUD's area office director to set the long-term occupancy at 95 percent, instead of the 93 percent used by the underwriter; the loan applicant would be able to obtain a larger mortgage.

The applicant submitted several letters from realtors where the proposed project was to be located, stating that vacancies were less than 5 percent. The area office director approved the use of a 95-percent occupancy level. The proposal was reprocessed and the mortgage amount increased by $132,400. The underwriter also decided that since a 95-percent occupancy level was approved, the loan applicant need no longer place $170,000 into escrow to cover the initial operating deficit originally forecasted. The file contained no documentation explaining the basis for this decision.

The project was completed in October 1974. By December 31, 1975, the project had achieved only 52-percent occupancy and incurred a $245,000 loss. The loan subsequently defaulted and was assigned to HUD in January 1976. HUD reported that the default was caused by a misjudgment of or change in the rental market. Occupancy increased to 93 percent by December 31, 1976. However, as of August 1977, HUD held the mortgage and the sponsor had failed to make 23 mortgage payments, amounting to about $660,000.

Project D

HUD insured this 225 unit section 236 (subsidized) project in August 1972 for about $4 million. Construction was completed in February 1974. Both the loan applicant and HUD's underwriter estimated occupancy would reach 95 percent during its first year of operation. The underwriter told us that HUD procedures specify that a 95-percent occupancy level be used. HUD procedures do not require that a predetermined occupancy level be used, and this matter is discussed on page 27. During 1975 (the first full year of operation) the project reached only 81-percent occupancy, resulting in $62,052 less income than estimated. The project has periodically defaulted since July 1976.

Expense estimates were often too low

Project operating expenses include costs for administration, maintenance, and operations and accounted for 63 percent of the total expenses for the 30 properties reviewed. Operating expenses are primarily made up of costs for gas, water, electricity and fuel oil (referred to as as utility expenses), taxes (mainly real estate, personal property, and employee payroll), and trash removal. Real estate taxes and utilities represent the bulk of projects' operating expenses. HUD rules require underwriters to estimate expenses by analyzing actual costs for similar projects.

Expenses actually incurred annually for 27 of the 30 projects exceeded by 5 to 110 percent the HUD-estimated expenses, as shown in the following chart. The dollar value of these differences ranged from $4,000 to $225,000. Expenses for the remaining three properties were over-estimated by 4 to 22 percent, or $2,600 to $17,000 annually.

	Extent to which expenses were underestimated annually			
Percent	Less than $10,000	$10,001 to $50,000	$50,001 to $100,000	Over $100,000
1 to 6	2	3	-	-
7 to 15	1	2	-	-
16 to 30	-	4	-	-
31 to 45	-	4	2	1
46 to 70	-	2	-	1
71 to 85	-	2	-	1
86 and over	-	-	-	2
Total	3	17	2	5

The primary difficulties involved the two largest expense elements--real estate taxes and utilities. Of 18 projects for which sufficient detailed information was available on utility estimates, HUD underestimated 17 by 9 to 146 percent, or $1,117 to $37,439 annually. Ten of 20 projects' real estate tax estimates for which detailed information was available were underestimated by 7 to 80 percent, or $2,755 to $104,616 annually.

The following examples describe the impact that underestimated expenses can have on a project's financial viability.

Project C

HUD insured this 478-unit section 221(d)(4) (non-subsidized) project in December 1972 for $9.7 million. Construction was completed in November 1974. The underwriter estimated first year occupancy would reach 70 percent; actual occupancy in 1975 reached 77 percent. Despite the unexpected increase in revenues, the project incurred a $220,440 loss in 1975 primarily because expenses exceeded HUD's estimate by $223,642, or 44 percent. Three expense items were substantially underestimated: real estate taxes ($116,865), administrative ($93,902), and utilities ($44,070). The project files showed that the underwriter based his estimates on actual operating results for four comparable projects as shown below:

Expense items (note a)	1975 actual	HUD estimate	Comparable projects No. 1	No. 2	No. 3	No. 4
Real estate taxes	$585	$340	$265	$589	$339	$335
Administrative	348	152	255	311	110	112
Utilities	277	184	310	196	174	146

a/Expenses expressed as per dwelling unit per annum.

The files contained no documentation to show how the underwriter arrived at the estimates, except to note that adjustments were made to recognize inflationary trend factors and differences in the size, age, location, and recreational facilities of the comparable properties. The underwriter who prepared the estimates is no longer employed by HUD. We reviewed the project files with another HUD underwriter who was unable to explain how the estimates were prepared.

The project defaulted in April 1976. HUD reported that the default was caused by a misjudgment of or change in the rental market. As of August 1977 the mortgage for the project had been assigned to HUD. The sponsor failed to make mortgage payments totaling over $500,000 to HUD at that time.

Project D

HUD insured this 145-unit section 236 (subsidized) project in January 1973 for $3.8 million. The underwriter estimated annual operating expenses of $118,260. Even though actual revenues were $30,097--11 percent more than forecasted--the project incurred a $29,138 deficit primarily because expenses were $102,762, or 87 percent more than HUD estimated.

The major expense items underestimated were real estate taxes ($36,765, or 80 percent), administrative ($30,384, or 176 percent), and utilities ($16,869, or 83 percent). Project files showed that the underwriter based his estimates on 1971 actual operating results for four comparable projects as shown below:

Expense items (note a)	1975 actual	HUD estimate	Comparable projects No. 1	No. 2	No. 3	No. 4
Administrative	$327	$118	$262	$217	$248	$286
Utilities	255	140	96	214	216	293
Real estate taxes	567	315	206	315	208	228

a/ Expenses expressed as per dwelling unit per annum.

The files contained no documentation to show how the underwriter arrived at the estimates. The underwriter who processed this project is no longer employed by HUD. The Chief of the Multifamily Valuation Section could not explain how the expense estimates were prepared or give reasons for the large variances between estimated and actual expenses. The project subsequently defaulted and the mortgage was assigned to HUD in December 1975. As of July 1977 the owners had failed to make mortgage payments of about $50,000.

Many of the projects examined are experiencing financial difficulty

As of July 1977, 21 of the 30 projects we selected for comparison of actual results with HUD estimates of income and expenses were experiencing financial difficulties.

Financial statements for these properties showed that operating expenses and debt service requirements were not being met because of insufficient funds. For 20 of the projects, financial difficulties surfaced during their first full year of operation--either 1974 or 1975. The remaining projects which were generating sufficient revenues had increased rents or achieved higher than expected occupancy levels.

As of July 1977, 9 of the 21 projects in financial difficulty had defaulted on their loans. Mortgage loans for eight of the nine projects were subsequently assigned to HUD.

ABSENCE OF DOCUMENTATION SUPPORTING UNDERWRITERS' ESTIMATES

Many multifamily project files did not document how underwriters arrived at estimates of project revenues and expenses. HUD procedures require that estimates be fully documented to provide assurance that they were properly prepared and reasonably accurate. Such documentation would also facilitate subsequent supervisory review.

At all three HUD area offices we visited, underwriters frequently failed to document how the estimates made were computed, as the following example illustrates.

Project E

A $2.7 million loan was insured by HUD in 1972 to rehabilitate this 183-unit section 220 apartment building. HUD's underwriter estimated expenses at $1,141 per dwelling unit annually. A list of 10 comparable properties in the underwriter's file showed expenses averaged $1,971 per unit, ranging from $1,350 to $2,787 per unit. The files contained no documentation describing how the underwriter reached the estimation of $1,141. Further, administration, operations, and maintenance expenses and taxes were not broken down by unit. The file also lacked documentation to show how revenues were computed, and whether inflation was considered. As of August 1977 this project had not defaulted.

Because multifamily projects cost millions of dollars to construct and the Government guarantees the mortgage loan in case of default, it is important that the estimates relied upon to approve project loans be fully documented.

PRIOR HUD AUDITS POINTED OUT WEAKNESSES IN ESTIMATING REVENUES AND EXPENSES

Some of these problems of estimating projects revenues and expenses were identified by HUD's OIG in 1972 and 1975. However, HUD has not aggressively attempted to correct these shortcomings.

--The January 1972 audit report pointed out that project operating expenses were consistently underestimated, unrealistically depicted maintenance expenses, and could influence the approval of an otherwise unsound project.

--The March 1975 audit report noted the need to improve techniques used to estimate operating expenses to arrive at more reasonable estimates.

OIG concluded that estimating errors were caused by such factors as:

--Data available for estimating project income and expenses was incomplete, and outdated and required adjustments.

--Supervisory review over the estimating process was inadequate.

--Little data was available at times on similar projects to use as a basis for making comparisons and estimates.

OIG also concluded that estimating errors were often caused by underwriters' failure to adhere to prescribed estimating techniques which required

--updating estimated taxes and operating expenses through the first year of occupancy,

--showing the impact of inflation through the first year of occupancy,

--examining actual operating data for at least three comparable projects, and

--documenting adjustments to data for comparable projects.

HUD's Office of Management responded to OIG on June 1, 1977, on findings still considered open by OIG as a result of its March 31, 1975, audit report. The Office of Management stated that it will issue a notice emphasizing the requirements for estimating expenses and will also emphasize proper estimation of operating expenses in its training courses.

In response to the finding on the inadequacy of data, the Office of Management stated that it has for several years designated people for data collection in all its field offices. Because of insufficient staff most field offices do not have such positions; consequently, underwriters must collect data on a case by case basis.

On December 16, 1977, OIG advised us that it evaluated the response to the findings, and many have not been resolved.

CHAPTER 3

OPPORTUNITIES TO INCREASE ACCURACY AND RELIABILITY OF UNDERWRITING ESTIMATES

HUD has taken some actions to improve its multifamily underwriting, but we believe that opportunities still exist to significantly increase the accuracy and reliability of estimates used to evaluate proposed project revenues and expenses.

HUD's major effort to improve underwriting through computerized data was inadequate and of questionable value to underwriters in preparing estimates. Usually, this data was inaccurate, incomplete, and outdated. As a result, underwriters had limited objective information to use as a basis for forecasting proposed projects' financial viability.

Other weaknesses in HUD's underwriting process identified during our review were:

--Property taxes--Contrary to HUD procedures, underwriters sometimes used property assessment methods and tax rates that were not applicable to the areas where proposed projects would be located.

--Occupancy rates--Some underwriters misinterpreted HUD procedures regarding occupancy rates by using a fixed rate for all projects in lieu of actual area occupancy conditions.

--Utility expenses--Underwriters did not aggressively seek the most current and reliable information for estimating major utility expenses.

--Inflationary trends--Underwriters used unrealistically low trend rates for analyzing project proposals.

--Cash flow--Many projects approved by underwriters did not provide for a sufficient cash flow margin to meet contingencies during the first few years of project operations.

In addition, the large-scale introduction in 1968 of subsidized multifamily housing programs for low- and moderate-income persons affected the manner and attitude of how some underwriters view their roles as well as the standards employed in the underwriting process. Some of the underwriters view HUD's primary objective in subsidized housing to be production, even though unrealistic underwriting estimates may be required so as to maintain the appearance of economically sound insurance risks. Such an attitude can reduce the effectiveness of an underwriting system to provide an objective and reliable measure for evaluating the elements of mortgage risk.

EFFORTS TO IMPROVE UNDERWRITING ESTIMATES BY COMPUTERIZATION--INEFFECTIVE

To improve underwriting estimates HUD computerized the process in November 1974. The objective was to speed up loan approval by providing computerized data on incomes and expenses for multifamily projects in operation. This data would be used as a basis for forecasting proposed projects' financial viability. Land values and actual construction costs were also computerized.

However, the computerized data underwriters used was inadequate and of questionable value in preparing estimates of revenues and expenses. Usually, it was inaccurate, incomplete, and outdated; either too little data was available for similar projects to use as a basis for making estimates and/or data that was available was incomplete and outdated.

Because of the poor quality of the data, in some cases, the underwriters were forced to make judgments in developing data for evaluating project proposals or to make adjustments to the only available computerized data which represented data of noncomparable projects.

HUD procedures state that if projects are to be processed within assigned target dates, it is essential that every field office have adequate banks of costs, valuation, marketing, planning, and mortgage credit data. Also, the procedures state that data must be continuously updated. Data accumulated through market studies, real estate brokers, property managers, mortgage lenders, contractors, builders, suppliers, and others are vital when screening proposed projects.

Moreover, the procedures state that it is imperative that all available data from HUD's Housing Management Division, such as financial statements from sponsors of projects already insured by HUD, be available and utilized in screening sponsor proposals. The underwriting staff should actively solicit from the Division all available information on operating expenses, taxes, occupancy, rent-up times, and any other relevant information to determine project feasibility.

Computerized underwriting system

This system is designed to provide information on operational projects comparable to the one being reviewed. Actual revenues and expenses for multifamily properties in operation are to be recorded in the system and maintained by HUD field office personnel. The underwriter is to use this data as an independent verification of sponsors' proposals and for developing income and expense estimates.

HUD area offices have terminals which provide access to the computer. The underwriter prepares a form listing the pertinent characteristics which best describe the proposed project--e.g., location, number of rental units, apartment dimensions, type of services, and equipment to be provided. The underwriter is then provided a listing from the computer of operational projects with characteristics most similar to the proposed project. The degree of similarity is expressed in percentages. Also, separate listings of operational data for comparable projects are provided by the computer, one each for income, expenses, and land values.

The underwriter can then adjust the comparable projects' income and expense elements to compensate for variances between the characteristics of the operational projects and the proposed project. For example, the size of apartments in the comparable projects might show a range from 735 to 835 square feet, while the size of apartments in the proposed project may average only 638. The underwriter would then make adjustments for the differences in the apartment sizes, after which the computer calculates future income and expenses for the proposed project using the underwriter's assumptions.

Accurate, complete, and current information not available

Decisions to insure multifamily loans are primarily based on underwriters' estimates of income and expenses, the accuracy of which depends heavily on the information in the computerized data base. We found the information in the data base to be inaccurate, incomplete, and outdated.

We performed various tests to assess the accuracy, age, and completeness of the data underwriters used at the three HUD area offices reviewed.

Accuracy of data bank information

In Chicago we examined expense and income data, physical characteristics of buildings, and site locations for 253 projects that were recorded on the separate files maintained for these items. Our analysis showed that 39, or 15 percent, of the projects on file were listed at site locations other than where they were actually located; 73, or 29 percent, had incorrect project ages recorded; 73, or 29 percent, had incorrect room dimensions recorded; and 30, or 12 percent, had the incorrect number of apartments recorded.

In Detroit we traced the expense data recorded in the computer files for 13 projects to source documentation, namely, the financial statements received from various projects in operation. Computer data differed from the source documentation for 12 of the 13 projects. For 7 of the 12 cases, the monthly expense data per dwelling unit ranged from $18 to $73 higher than the data recorded in computer files and $88 lower in 1 instance. In the remaining four cases, the variances in the expense amounts offset each other.

In late 1975 the San Francisco area office purged its computer data base and initiated steps to obtain accurate and reliable information for use in evaluating proposed projects. Area office officials told us that the old data base was inaccurate and much of the expense information was recorded in incorrect categories or was insufficiently broken down so as to be useful in analyzing proposed projects. San Francisco's computer data base contained limited information at the time of our review. Officials told us they were entering new data into the computer and verifying it to insure accuracy.

Completeness of data bank information

As previously discussed, each area office is required to maintain a computer data bank with adequate information for evaluating project proposals. Also, HUD underwriters are required to actively solicit all pertinent information in evaluating project proposals.

In Chicago complete information was not available to underwriters in evaluating proposals. The computer data bank contained income information for 686 projects, whereas the expense data bank contained information on only 253 projects. Also, the computer bank did not include project income data for 6 counties and expense data for 3 counties of the 19 counties that make up the area serviced by the Chicago area office. Without this information the computer, in one case, selected project expense data for a project located about 160 miles from a project being proposed for the Chicago area.

In addition, the data banks contained little financial information for privately financed projects. For instance, HUD's computer bank had expense data for only four conventionally financed projects. The opportunity to obtain more expense information on privately financed projects is available since there are over 12,000 such projects in the Chicago area.

In Detroit the completeness of information in the computer data banks was adversely affected because financial operating statements from HUD-insured projects were not submitted within the prescribed time as discussed on page 23. In San Francisco, as previously discussed, the computer data banks were purged, and that office was in the process of obtaining more complete and reliable information.

Currency of data bank information

HUD regulations require that mortgagors of multifamily projects insured under its programs submit annual financial statements within 60 days after the close of their fiscal years. Also, HUD requires each area office to establish the necessary controls to identify and follow up on the submission of delinquent financial statements. This information is partially used to maintain the computerized underwriting system.

During our review we requested the San Francisco and Chicago officials to give us a list of projects making up the expense data files. In Chicago, 52, or 21 percent, of the 253 projects' expense data on file was 1 year or more old. In some cases, more current financial statements had been submitted to HUD personnel in the loan management section but had not been forwarded to underwriters for updating the computer base.

Also, in Detroit, 25 of the 46 HUD-insured multifamily projects we tested had not submitted financial statements as required.

Effect of inadequate computer data

Because the computer data banks contain inaccurate, incomplete, and out-of-date information, underwriters' evaluations of sponsors' proposals are more difficult because less reliable objective data is available and more judgment is required in revising the computer estimates to use them for comparative purposes. Also, as previously discussed, the adjustments underwriters make were generally not documented; hence, management has little assurance that approval of projects was based on accurate and reliable information. Use of the best available financial operating data of multifamily projects similar to the proposed project enhances the reliability of income and expense estimates.

The computer is programed to compare the physical characteristics for certain operational projects to the proposed project and provide the underwriter with a list of comparable projects. Physical characteristics considered are geographic location, number of dwelling units, number of bedrooms, room dimensions, equipment, and services provided. Each characteristic has a maximum weight. For example, in the selection of expense comparables, geographic location has a maximum weight of 30, whereas average room dimension has a maximum weight of 5. The computer then searches its files, scores each project, and lists five projects with the highest score (expressed as a percentage). The percentage reflects the degree of similarity, or comparability, of the operational project to the proposed project.

The following examples illustrate the (1) type of computer data available to underwriters for evaluating sponsors' proposals and (2) need for underwriters to make significant judgments in revising data to make it more comparable.

Project F

HUD insured a $1.4 million loan to construct this 7-building 42-unit, 1- and 2-bedroom apartment complex in June 1976. Rents and expenses were estimated on the basis of various operating properties. The underwriter was provided with information which showed a minimal degree of comparability between the proposed project and projects for which operational data was on file in the computer. The comparable projects used to estimate rents ranged in degree of comparability from 44 to 67 percent for one-bedroom units and from 47 to 70 percent for two-bedroom units. Comparable projects used for estimating expenses were less comparable, ranging from 38 to 48 percent.

In June 1976 the underwriter concluded that a one-bedroom unit would rent for $316 per month on the basis of the comparable data in the table below:

Comparison of project amenities	Proposed project	Comparable projects 1	2	3	4	5
Rent	$316	$240	$265	$255	$245	$245
Average size (square feet)	638	735	800	750	835	835
Swimming pool	No	Yes	No	Yes	Yes	Yes
Heating provided	No	Yes	Yes	Yes	Yes	Yes
Cooking gas provided	No	Yes	No	No	Yes	Yes
Hot water provided	No	Yes	Yes	Yes	Yes	Yes
Water provided	No	Yes	Yes	Yes	Yes	Yes
Degree of comparability of the properties (percent)		67	65	51	47	44
Date of financial data on comparable properties		2/75	12/75	9/75	9/75	7/75

There was no further documentation to show how the underwriter concluded that the one-bedroom units would rent for $316, except that project records showed that the project was to be located in a desirable residential area--not far from downtown and commuter stations.

However, much judgment would be required in arriving at revenue and expense estimates because the projects available for comparison had different amenities, equipment, and services included in rent payments and were not located in the same area as the proposed project.

Project G

HUD insured a $4.9 million loan to construct this 170-unit apartment building for the elderly, which was expected to begin operations in 1977. Rents were based on six projects which were only 30 to 53 percent comparable. Expenses were based on projects which were only 42 to 49 percent comparable.

In this case also, the underwriter made many adjustments to reflect differences in location, mix of apartments, room sizes, services, and amenities. Of the five projects in the computer only one was located near the site of the proposed project. The proposed project was to contain efficiencies and one-bedroom apartments; the comparables were a mix of one-, two-, and three- or more bedroom apartments. The average size of the proposed apartments was 618 square feet each; the comparable data was for apartments that ranged from 518 to 748 square feet. The proposed project planned that the tenant would pay for utility expenses; some of the comparables included these expenses in the monthly rental charge.

Reasons for estimating errors

We asked HUD officials at the three area offices reviewed about the computer banks' inaccurate, incomplete, and out-of-date information. They generally agreed that these deficiencies existed and had posed problems in providing meaningful project data to underwriters for evaluation purposes. They also offered the following reasons for the problem:

--A lack of staff to properly maintain computer data banks.

--A lack of adequately trained underwriting staff.

--A general attitude in one area office that projects should be examined in their most favorable light, and approved, if at all possible.

FAILURE TO ADHERE TO PRESCRIBED UNDERWRITING PROCEDURES

HUD underwriters were not following underwriting procedures when estimating property taxes. Although HUD procedures require them to become fully informed about local practices when assessing property taxes, they at times used property assessment methods and tax rates not applicable to the areas in which the proposed project would be located.

Because the methods assessors use in arriving at the assessed value of real property vary so widely, HUD procedures state that it is imperative for the underwriter to obtain complete information to enable a fair estimate of future taxes. The underwriter is to become fully informed about local practices and mechanics for assessing property. An estimate, prepared on the basis of the local tax assessor's method, is then to be compared to actual current taxes for comparable properties, according to the procedures.

All three HUD area offices had difficulty in estimating realistic real estate taxes. We selected three projects approved by the Detroit area office to determine how taxes were estimated. We found that HUD had significantly underestimated real property taxes from 35 to 52 percent for the three properties as shown below. In making our comparisons we obtained from the local tax assessor the applicable methods being used and rates prescribed for the jurisdiction where the properties were to be located.

	Project 1	Project 2	Project 3
GAO estimate	$29,100	$53,086	$194,410
HUD estimate	21,537	34,964	144,038
Difference	$ 7,563	$18,122	$ 50,372

These differences occurred because HUD underwriters used incorrect property assessment methods and outdated tax rates. The following example illustrates the differences between the estimates we prepared and those of the underwriter, with the assistance of officials in a local tax assessor's office. At the time of our review, this project had not been operating long enough to obtain actual tax costs.

Project 1

On May 14, 1976, the underwriter estimated, but could not explain why, real property taxes on this multifamily project would be $21,537, computed by multiplying an assessed value of $408,213 by $52.76 tax rate per $1,000 of assessed value.

A local tax assessor's office representative told us that the income approach method was used in this location to establish assessed value for tax purposes. This method is based on the amount a potential purchaser would be willing to pay for the right to earn a certain net income from that property over a period of years. Also, this representative said that the 1976 real property tax rate effective January 1, 1976, for this location was about $61, not $52.76. Using the income approach, we assessed the value at $477,050--$68,837 more than the underwriter's estimate. After applying the $61 rate per $1000, the real property tax would be $29,100--$7,563 more than estimated.

MISINTERPRETATION OF OCCUPANCY RATE PROCEDURE

As discussed on page 9, many of the revenue estimates made by underwriters were not achieved because of higher vacancy rates than estimated following the initial rent-up period. Underwriters were misinterpreting HUD occupancy rate procedures by using fixed-occupancy rates for all projects in lieu of actual data on vacancy rates, which indicated that a much lower occupancy rate should have been used.

We believe it is unrealistic to use fixed occupancy rates for all projects because local area conditions cause occupancy rates to vary by location. In this regard the 1975 edition of "Income/Expense Analysis" 1/ showed that average vacancies and rent collection losses varied from about 4 to 11 percent nationwide in 1974.

At the three HUD area offices visited, the underwriters usually estimated that occupancy rates would be 93 percent for nonsubsidized and 95 percent for subsidized properties after the initial rentup period. HUD officials at these offices told us that these occupancy levels were prescribed by HUD procedures.

However, the guidelines these individuals cited did not require that fixed rates be used for estimating occupancy rates; rather, they state that occupancy rates

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1/A publication by the Institute of Real Estate Management, 1975 edition.

seldom exceed 93 percent for nonsubsidized projects and although it is likely that a 93-percent occupancy level will be achieved, local conditions may dictate the use of a lower rate.

MORE RELIABLE INFORMATION AVAILABLE FOR ESTIMATING KEY COSTS OF UTILITIES NOT CONSIDERED

HUD procedures require that underwriters estimate utility expenses on the basis of actual expenses paid for comparable properties. They also state that underwriters should aggressively seek all available information in preparing such estimates.

Generally, underwriters used information in the computerized data base to obtain utility costs for comparable projects and made adjustments for inflationary trends in arriving at utility estimates. Although several sources exist which provide information on utility costs, including various organizational units within HUD and utility companies, we found little evidence that underwriters actively sought these sources and/or considered their utility cost information.

The Architectural and Engineering Division within the area offices (not part of the underwriting units) are required to prepare prototype utility analyses consisting of various utility combinations and fuel types for buildings of various styles, sizes, and types of construction for various HUD programs. The analysis is (1) performed to determine the most economical method of providing such services and (2) required to be updated annually or when rates or other cost factors change.

The following example illustrates the need for the underwriters to seek pertinent utility cost data available within HUD when preparing utility estimates.

Project H

The underwriter in May 1976 prepared the utility expense estimate for gas heating and hot water service on the basis of 1973 financial data for three comparable properties. This data showed that annual costs per dwelling unit for gas service varied significantly: property one--$62, property two--$90, and property three--$115, or an average of $89. The underwriter used $85 plus 20 percent for inflation to compute the utility expense estimate for the 41-unit apartment building--$4,182 per year. A prototype utility analysis prepared by the Architectural and Engineering Division for a property similar to the proposed project showed that the same gas service would be about $226 per dwelling unit. Use of the $226 figure indicates that the utility expense would be more than double ($9,266) what the underwriter estimated.

Another source of information underwriters should consider is utility cost analyses made for section 8 projects. 1/ Each area office prepares fair market rent determinations for this program which include estimates on utility costs for newly constructed or substantially rehabilitated units. These estimates are prepared annually or more frequently as warranted.

Utility cost information is also available from utility companies. We contacted electric and gas company representatives servicing the Chicago area. They told us that they have actual consumption data for all apartment buildings in their service area as well as firsthand knowledge of impending and forecasted changes. They also said that builders and contractors frequently ask them to estimate utility expenses, and they would be willing to provide similar information to HUD if requested.

NEED TO STANDARDIZE METHOD FOR PROJECTING INFLATION

HUD procedures recognize the need for underwriters to consider inflationary trending factors when analyzing a proposed project's rental and operating expense estimates. The procedures state that inadequacies in expense estimates are often attributable to improper trending of estimates. In projecting estimates, the procedures require underwriters to take into account the age of the data of comparable properties used, loan processing and construction time, and the time frame required to complete the first year of project operation.

However, the procedures specify neither the source for inflationary trending factors to be used nor the methodology for deriving them. As a result, underwriters used unrealistically low inflationary rates for analyzing project proposals; hence, the impact of inflation on some project expenses was at times underestimated.

1/Section 8 is currently HUD's major program to subsidize lower income families to help them afford decent private market housing.

For example, in Chicago, underwriters derived their own trend factors individually and the rates used represented their judgment.

We compared the trend factors used by HUD underwriters for four Chicago projects with the changes in the Consumer Price Index for housing 1/ for the estimated period. The four estimates were prepared within a 6-month period for projects to be located in the same area. The impact of inflation varied and was understated as shown below:

Monthly trend period	Percentage of HUD trend factor	Percentage of change in Consumer Price Index
48	6	36
40	7	30
37	7	27
37	7	22

In the absence of supporting documentation, we could not determine how the underwriters arrived at estimated trends. The following example illustrates how trend factors were applied to estimates for an apartment project underwritten by the Chicago area office.

Project I

HUD insured a $4.3 million loan for an 11-building 253-unit section 221(d)(4) apartment complex located in a Chicago suburb. The underwriting was completed in December 1972. HUD used a 7-percent trend factor for expenses to cover a 37-month trend period, the equivalent of about 2 percent annually. The Consumer Price Index for housing increased 27 percent, or about 8 percent annually, during this period. Had a more realistic trend factor been used, HUD would have been in the position of questioning the feasibility of the project as proposed. Subsequently, the loan defaulted and was assigned to HUD. HUD reported that the default was caused by a substantial increase in expenses.

In San Francisco, individual trend factors for rents and individual expense items were developed for use by all underwriters. The trend factors used were derived from

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1/This index includes such items as fuel, utilities, mortgage interest, taxes, and home maintenance and repair costs.

historical data for specific geographic areas. Also, the Chicago area office director agreed that more reliable rates could be developed.

During our review Chicago area office underwriters began using standardized inflationary trend factors for rents and expenses. For rents, they are required to use the trend factors used for periodically updating fair market rents under the section 8 housing program. Also, they have developed data for various expense items for guidance in determining trend factors.

SHOULD HUD ESTIMATES OF PROPOSED PROJECTS PROVIDE FOR SAFETY MARGIN?

As previously discussed, most multifamily projects default because of insufficient cash flow to meet operating expenses and to cover debt service. Of the 30 project estimates examined, 19 failed to provide for sufficient cash flow to cover any subsequent deviations between the estimated and actual revenues and expenses.

Because underwriting is not a precise science and some variances can be expected when actual revenues and expenses are compared to underwriting estimates, we believe that HUD should consider establishing a safety margin in its estimating phase to provide for a safety margin in cash flow. What is a margin for error? Making adequate provision in the estimates for contingencies so that sufficient cash will be available to pay expenses and mortgage debt service. HUD underwriters forecasted cash flows of only 2 to 6 percent of gross revenues for the aforementioned 19 projects. In short, the projects' cash flows are planned too close. Limited cash was available to meet unforeseen problems, such as lower occupancy levels than estimated.

For example, cash flows of 6 percent or less were typically predicated on the basis that a 93-percent occupancy rate would be attained. Hence, failure to obtain an occupancy rate of 87 percent or more will result in a deficit--assuming expense estimates were accurate.

The San Francisco Regional Office contracted with the Berkeley Planning Associates to study the financial failure in multifamily subsidized housing projects, which included a synthesis of conclusions and recommendations contained in previous reports. In a report dated July 1975, the Associates concluded, in part, that:

"If budgets are set this tightly, then either they are unrealistic or the project management must be routinely expected to be extraordinarily effective both in collecting rents and holding down costs. It appears that operating cost and revenue estimates have been technically faulty or forced to make projects feasible. Where the underestimation was done by developers, HUD did not challenge it. The resulting financial instability creates a situation where projects need rent increases as soon as they begin operation. No margin is left for mistakes or unexpected events * * *."

While there are advantages in providing a safety margin, we recognize that such a requirement contains certain disadvantages from the standpoint of sponsors, i.e., they may be required to initially put more cash into the project or specified dollar amounts may be required to be placed in an escrow account for a specified time. Because HUD estimates of project revenues and expenses are presently prepared with little margin for error and often insufficient cash flow is generated after a project is operating, we believe that HUD should study the feasibility of requiring a safety margin when evaluating and approving proposed projects.

NEED TO REEMPHASIZE UNDERWRITING FUNCTION

The large-scale introduction in 1968 of HUD-subsidized multifamily housing programs for low- and moderate-income persons affected the manner in which some underwriters view their roles as well as the underwriting process standards. Some underwriters seem to view HUD's primary objective in subsidized housing to be producing housing, even though unrealistic underwriting estimates may be required so as to maintain the appearance of economically sound insurance risks. Such an attitude can corrode an underwriting system that is needed to objectively and accurately evaluate the elements of mortgage risks.

During congressional hearings in September 1977, the Secretary of HUD indicated that the benefits of housing assistance include significant contributions to community development and neighborhood revitalization in our cities. Also, she said that preventing the deterioration of housing and upgrading of blighted or deteriorating neighborhoods are essential parts of any successful urban revitalization strategy.

HUD's report entitled "Housing in the Seventies" of November 1974 stated that the passage of each new insurance program has resulted in more liberalization of mortgage terms and underwriting principles because the:

--"Economic soundness test" for the proposed construction has been replaced with an "acceptable degree of risk."

--Mortgage amount changed from being based upon a more conservative estimate of long-range market value to "replacement cost."

--Maximum loan amount has been increased and, in some cases, the term of the mortgage extended, thereby permitting lower monthly payments.

An independent study sponsored by mortgage bankers, realtors, savings and loan institutions, and the home building industry on "Public Subsidized Housing and Private Mortgage Lending," issued in July 1976, noted among other things, the following about underwriting:

> "Inherently there seems to us a contradiction in applying an insurance concept to a non-economic project. Subsidy in itself has to be considered a form of insuring the success of a project by creating a market. In fact, it may create a subsidized market, but it does not assure the success of the project.
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> "Forcing the underwriting decision to take on the look of an economically sound insurance risk not only is corrosive to the underwriting process but results in an entirely false exercise."

This report suggested that criteria for economically sound mortgage insurance systems apply to nonsubsidized properties only. Further, the report previously mentioned (see p. 31) on multifamily housing project failures by the Berkeley Planning Associates attributed the cause for poor HUD underwriting estimates to meeting production goals.

> "Estimates of operating expenses have been cursory and inaccurate, the commendable desire to get projects built within program constraints leading to the acceptance of unrealistic estimates and generally to discounting inflation."

The following comments made by HUD underwriting officials during our review indicated that some of them believe that meeting housing production goals is the ultimate measure of success and that proposed projects should be viewed in their most favorable light.

--San Francisco area office officials said that the reason expense estimates were so poor was that the general attitude in their area office was that projects should be examined in their most favorable light, and approved, if at all possible.

--The Chief of an Economic and Market Analysis Division told us that he can only give an opinion whether there is a market for a property. However, top management made the decision and since the name of the game is production, his opinion that no market exists is at times rejected.

--A chief underwriter told us that he believed that HUD should be evaluated on the number of construction starts. If congressionally established housing goals are to be met, then risks must be taken and the results accepted.

Regarding one project in California, HUD officials told us that it was approved to meet an overriding social goal contrary to the dim financial forecast provided by the underwriter. Although not a subsidized project, it does illustrate why projects are at times approved for insurance regardless of underwriting estimates and why perceptions that projects should be viewed in their most favorable light have come about.

<u>Oakland, California</u>--A $5.2 million section 220 (nonsubsidized) loan for an 18-story 178-unit apartment building in this city was approved by HUD against the advice of its underwriters:

--The market for such luxury apartments was considered to be saturated, rents were too high, and the rentup period too long (estimated to take 2-1/2 years).

--The sponsor had a bad track record--one other project had defaulted.

The Operations Division Director and the Real Estate and Valuation Section Chief told us that it was more important to fulfill HUD's social goal of turning around a decaying urban area than adhering to sound underwriting practices. HUD had spent millions of dollars in attempting to change Oakland's image and these officials felt it would be inconsistent to reject this proposal. However, both officials agreed that the project should not have been approved on the sole basis of underwriting determinations. In 1975 the mortgagor defaulted on the loan. The 95-percent occupancy rate had not been attained, averaging only 44 percent from November 1975 through June 1976 and reaching a high of 75 percent in October 1976. As of August 1977 the mortgage had been assigned to HUD.

CONCLUSIONS

In recent years HUD has incurred a string of financial losses due to mortgage defaults, foreclosures, and assignments on its multifamily loan insurance programs. The problems which caused the failures of multifamily projects are complex, and no one solution is likely to be developed which will ameliorate the situation. Moreover, the need for Federal programs to aid low- and middle-income families in obtaining good quality shelter which they otherwise could not afford or obtain, coupled with the need to transform badly deteriorating inner-city housing into economically viable areas, are major concerns of Federal, State, and local officials. Hence, it is likely that Federal programs will continue to be directed at these problems.

While some losses are unavoidable, we believe that opportunities exist to improve the accuracy and reliability of computerized information underwriters use to evaluate sponsors' proposals, to obtain greater compliance by underwriters with certain estimating techniques and to clarify others, and to reemphasize the importance of the underwriting role.

We recognize that weaknesses in techniques used to estimate multifamily projects revenues and expenses do not solely explain why multifamily projects default. However, we believe that correcting these weaknesses will result in more accurate underwriting estimates and better assessments of proposed projects' financial soundness.

Accurate estimates of operating results also afford HUD an earlier opportunity to identify alternatives for improving the financial viability of higher risk proposals. Once a project is approved for mortgage insurance, HUD's options are reduced to essentially increasing rents and/or providing a moratorium on the interest and principal payments for a short-term period. On the other hand, before the mortgage is approved, HUD can require that the project scope be revised, the sponsor can put more money into the project, an escrow account can be established for possible future contingencies, or the proposal can be rejected.

RECOMMENDATIONS

To better assess the financial soundness of multifamily projects proposed for insurance, we recommend that the Secretary of HUD:

--Insist that field offices maintain accurate, complete, and up-to-date financial and project characteristic information in the computer base used to evaluate proposed projects, including assigning adequate staff with proper training to implement underwriting objectives.

--Insist on underwriters' strict adherence to underwriting procedures for preparing real estate tax estimates, aggressively seeking information on utility costs, and maintaining documentation to support estimates of project revenues and expenses.

--Require that uniform methodologies be devised and used in projecting the impact of inflationary trends on proposed projects.

--Clarify procedures regarding estimating occupancy levels.

--Examine the possibility of establishing a safety margin which would increase cash flow to cover contingencies during the first few years after a project becomes operational.

--Reemphasize the importance of the underwriting function in objectively and accurately evaluating elements of mortgage risk.

AGENCY COMMENTS AND OUR EVALUATION

In a January 23, 1978, letter, HUD's Assistant Secretary for Housing-Federal Housing Commissioner agreed with our recommendations. (See app. I.) He said that it is clear that past emphasis upon production resulted in inattentiveness to basic underwriting principles in some areas. While he agreed wholeheartedly that production should not, and need not, be accomplished at the expense of quality, he said the difficulty of achieving the proper balance must be recognized. In response to our recommendations, the Assistant Secretary said HUD plans to:

--Strengthen headquarters monitoring of field offices' maintenance of accurate, complete, and up-to-date financial and project characteristic information in the computer base used to evaluate proposed projects. Also, this matter will be brought to the attention of HUD's field staff. In addition, training centers have recently been reopened in specific disciplines to develop better trained personnel for future processing roles.

--Emphasize through notices and training the need for accurate real estate and utility cost estimates, including the mandatory requirement that such estimates be fully supported by complete, detailed documentation.

--Issue clarified updated instruction requiring that uniform methodologies be used in projecting the impact of inflationary trends on proposed projects.

--Emphasize to its field personnel the need to follow procedures for computing occupancy levels.

--Study the possibility of establishing a safety margin to increase projects cash flow.

--Reemphasize to its field staff underwriters the importance of objective underwriting.

The Assistant Secretary also commented that while the report does warn of problem areas in the underwriting process which need attention, much of what has occurred during the time frame of this report was unpredictable by the most conservative of underwriters.

He pointed out that the sampling used 30 to 50 projects with commitments issued between July 1, 1972, and June 30, 1976, which represented housing production that occurred during the very worst years of inflation and energy shortages. Double digit inflation, escalating utility costs, and taxes could not be foreseen to the extent they occurred, nor will any future underwriting system provide such foresight. Nor did anyone, including the country's best economists, anticipate the stagflation that occurred in 1974 and a prime interest rate at a level of 12 percent. The Assistant Secretary said that our final conclusions are therefore subject to interpretation.

As discussed in our report, we recognize that underwriting is not a precise science. Many factors have to be evaluated, and the accuracy of estimates can be affected by unpredictable events, such as strikes and rapid changes in the economy. We believe, however, that to the extent that objective, accurate, and reliable estimates are made and used to evaluate proposed projects, better assessments can be made of the financial soundness of such projects and the Federal Government has a greater selection of options before insuring a mortgage.

With regard to the projects sampled, two separate samples are used in our report. One sample of 30 projects was made to identify problems experienced in underwriting multifamily projects. These projects were selected on the basis that HUD had made firm loan commitments between July 1, 1972, and June 30, 1976, and the projects had been in operation for at least 1 full year. The other sample of 16 additional projects was used to evaluate HUD's multifamily underwriting process. These projects were selected on the basis that underwriting had just been completed at the time of our review.

The Assistant Secretary also said that while the report cites instances of apparent disregard of underwriting procedures, it fails to specify the projects used for the analysis, thus making it impossible to determine the significance of the reported discrepancies in the total transaction.

We focused on assessing the accuracy of underwriting estimates of project incomes and expenses. Our analysis of certain income and expense items, such as occupancy, utilities, taxes, and inflation trends, showed wide variations between the HUD estimates and the actual revenues and expenses experienced by the projects. However, we did not attempt to relate these specific variances to the financial statements on an individual project basis. Rather, we concentrated on identifying specific steps HUD could take to improve its techniques for estimating individual revenue and expense items and thereby reduce the degree of risk associated with insuring costly multifamily projects.

With regard to the significance of the reported underwriting discrepancies in the total transaction, 21 of 30 projects reviewed had been in serious financial difficulty as of July 1977. (See p. 7.)

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, D.C. 20410

OFFICE OF THE ASSISTANT SECRETARY FOR
HOUSING-FEDERAL HOUSING COMMISSIONER

IN REPLY REFER TO:

JAN 23 1978

Mr. Henry Eschwege
Director, Community and Economic
Development Division
United States General Accounting Office
Washington, D. C. 20548

Dear Mr. Eschwege:

Your letter of November 9, 1977, addressed to the Secretary of Housing and Urban Development, transmitting a proposed report to the Congress entitled: "Need to Better Assess Financial Soundness Before Insuring Multifamily Residential Properties," has been referred to me for reply.

While the report cites instances of apparent disregard of established underwriting procedures, it fails to specifically identify the projects used for the analysis, thus making it impossible to determine the significance of the reported discrepancies in the total transaction. Further, the sampling used 30 to 50 projects with commitments issued between July 1, 1972 and June 30, 1976, which represented housing production that occurred during the very worst years of inflation and energy shortages. Therefore, the final conclusions embodied in the draft are subject to interpretation. Underwriting has as its basis trends and economic predictions, such as the cost of materials which, if they do not come to pass due to economic abnormalities, will undermine the soundest underwriting calculation. Nevertheless, the report does serve as a warning note of problem areas in the underwriting process which need attention.

I will respond to the specific recommendations in the order that they are presented.

Recommendation No. 1: To better assess the financial soundness of multifamily projects proposed for insurance, the Secretary of HUD should insist that field offices' maintain accurate, complete, and up-to-date financial and project characteristic information in the computer base used to evaluate proposed projects including assigning enough staff of proper training to carry out HUD's underwriting objectives.

Reply: This is not a new problem but is one of which we have been aware for some time. Existing instructions do require the maintenance of proper data, periodically updated. This requirement has been periodically brought to the attention of field staff and we intend to do so again in the immediate future. We are also anticipating the strengthening of headquarters monitoring activities in this area. We continually provide training for our field technical processing staff and have recently reopened training centers in specific disciplines to develop better trained personnel for future processing roles.

Recommendation No. 2: To better assess the financial soundness of multifamily projects proposed for insurance, the Secretary of HUD should insist on underwriters' strict adherence to underwriting procedures relating to preparing real estate tax estimates, aggressively seeking information on utility costs, and maintaining documentation to support estimates of project revenues and expenses.

Reply: We concur in this recommendation and will remind all staff, through notices and in training, of the absolute necessity to obtain and use accurate real estate tax and utility costs estimates. We will also emphasize that it is mandatory that all estimates be fully supported by complete, detailed documentation.

Recommendation No. 3: To better assess the financial soundness of multifamily projects proposed for insurance, the Secretary of HUD should require that uniform methodologies be developed and used in projecting the impact of inflationary trends on proposed projects.

Reply: We concur in this recommendation and will issue clarified, updated instructions in this area at an early date.

Recommendation No. 4: To better assess the financial soundness of multifamily projects proposed for insurance, the Secretary of HUD should clarify procedures regarding estimating occupancy levels.

Reply: As the report points out, the instructions are now clear, it is their application that has been criticised. Nevertheless, we will call this matter to the attention of field personnel.

Recommendation No. 5: To better assess the financial soundness of multifamily projects proposed for insurance, the Secretary of HUD should examine the possibility of establishing a safety margin which would increase cash flow to cover contingencies during the first few years after a project becomes operational.

Reply: This is a matter which we are looking into. We must not, however, unnecessarily increase the cost of development and the ability of sponsors to provide needed housing under our programs.

Recommendation No. 6: To better assess the financial soundness of multifamily projects proposed for insurance, the Secretary of HUD should re-emphasize the importance of the underwriting function in objectively and accurately evaluating elements of mortgage risk.

Reply: The recommended reemphasis will be made.

We appreciate the concern of the General Accounting Office over the reported deficiencies found in the underwriting process. While we agree wholeheartedly that production should not, and need not, be accomplished at the expense of quality, we must recognize the difficulty of achieving the proper balance. It is clear that past emphasis upon production resulted in inattentiveness to basic underwriting principles in some cases. However, much of what has occurred during the time frame of the report was unpredictable by the most conservative of underwriters. Double digit inflation, escalating utility costs and taxes could not be foreseen to the extent they occurred, nor will any future underwriting system provide such foresight. Nor did anyone, including the country's best economists, anticipate the "stagflation" that occurred in 1974 and a prime interest rate at a level of 12 percent. This, of course, does not minimize our responsibility to properly underwrite, at the same time achieving our social goals. It is our intention to take whatever corrective action may become apparent, within the limits of our budgetary authority.

Sincerely,

Lawrence Simons

Lawrence B. Simons
Assistant Secretary

DESCRIPTION OF HUD MULTIFAMILY

PROGRAMS REVIEWED

Section 207 program

The National Housing Act of 1934 authorized the insurance of mortgages under section 207 (12 U.S.C. 1713) to facilitate the production of good quality housing that would serve the needs of a broad cross section of the rental housing market at reasonable rents.

The section 207 program is HUD's basic nonsubsidized rental housing program, under which HUD is authorized to insure privately financed mortgage loans for the construction and/or rehabilitation of economically sound multifamily rental projects. Eligible mortgagors include investors, builders, developers, and others who meet HUD-FHA requirements for mortgagors. The maximum insured loan amount, in most cases, is limited to 90 percent of the project's estimated value.

The section 207 mortgage insurance program is carried out under the General Insurance Fund, details of which are discussed on page 45.

Section 220 program

The Housing Act of 1954 amended the National Housing Act by adding section 220 (12 U.S.C. 1715k) which authorized a program to aid in eliminating slums and blighted conditions and preventing the deterioration of residential property. This program was intended to supplement mortgage insurance under sections 203 and 207--HUD's basic nonsubsidized single and multifamily programs, respectively.

Under the section 220 program HUD insures mortgages for the rehabilitation of existing structures and new construction in an approved urban renewal area, an urban redevelopment project, a code enforcement program, or an urban area receiving rehabilitation assistance as a result of a natural disaster. The section 220 program is carried out under the General Insurance Fund.

Section 221(d)(3) and section 221(d)(4) programs

The Housing Act of 1954 amended the National Housing Act by adding section 221 (12 U.S.C. 1715(l)) a program designed to meet the needs of low- and moderate-income families, as well as families displaced from urban renewal areas or as a result of governmental action.

Under these programs HUD is authorized to insure loans to construct or substantially rehabilitate multifamily rental or cooperative housing projects. Currently, the principal differences between the two programs are:

--HUD will insure 100 percent of project value under section 221(d)(3) but only 90 percent under 221(d)(4).

--Nonprofit (or limited-dividend or cooperative) organizations may qualify for 221(d)(3) mortgages, while 221(d)(4) mortgages are reserved for profit-oriented sponsors.

Formerly, the two programs were distinguished by the following differences. Projects financed under section 221(d)(3) could qualify for below market interest rates (as low as 3 percent) and for rent supplements. These are Federal payments which reduce rents for certain disadvantaged low-income persons. Below market interest rates and rent supplements are no longer available for new projects insured under these programs. The rent supplement program was suspended under the housing subsidy moratorium of January 5, 1973. However, units financed under both programs may now qualify for assistance under the section 8 program. This is currently the Federal Government's major program to subsidize lower income families to help them afford decent private market housing. The section 221 programs are carried out under the General Insurance Fund.

Section 236 program

The Housing and Urban Development Act of 1968 (42 U.S.C. 1441a) amended the National Housing Act by adding section 236 (12 U.S.C. 1715z-1)--a program to provide low- and moderate-income multifamily rental housing units.

HUD is authorized to insure privately financed mortgage loans to construct or substantially rehabilitate multifamily housing projects and to pay, on behalf of the mortgagors, the mortgage insurance premiums and the interest on the mortgage loans over 1 percent.

On January 5, 1973, HUD suspended the section 236 program along with other federally assisted housing programs. However, considerable expenditures under the program will continue for many years because of many units already in operation. HUD estimates that interest reduction payments on existing projects could amount to about

$10.3 billion over the remaining life of these project mortgages. Current activity under this program consists mainly of funding bona fide commitments issued before the program was suspended. Insurance operations are carried out under the Special Risk Insurance Fund, which is further discussed on page 46.

DESCRIPTION OF HUD'S FOUR MORTGAGE INSURANCE FUNDS

MUTUAL MORTGAGE INSURANCE FUND

The Mutual Mortgage Insurance Fund (MMIF) was established under the authority of section 202 of the National Housing Act. Mortgages of small homes are financed under this fund. Section 205 of the act:

--Authorized the establishment of a Participating Reserve Account and a General Surplus Account in MMIF.

--Provided that both accounts be available to meet losses arising from MMIF insurance operations.

--Authorized allocation of the income or loss from operations in any semiannual period to either or both accounts and to distribute as dividends a share of the Participating Reserve Account to mortgagors after the MMIF-insured mortgage loans have been paid. However, mortgagors have no vested rights in the account.

--Required that the allocation of the income or loss and the distribution from the Participating Reserve Account be made in such a manner and amount as to be in accord with sound actuarial and accounting practices.

GENERAL INSURANCE FUND

The General Insurance Fund (GIF) was established on August 10, 1965, under the authority of section 519 of the National Housing Act, as amended, to implement the mortgage insurance programs authorized by several sections of the act. GIF is used to insure mortgages under various programs, including some high-risk insurance programs that might have been made part of the Special Risk Insurance Fund if it had existed when these programs were enacted. The GIF deficit is attributable to the high-risk insurance programs. GIF is used to insure mortgages and notes that enhance the purchase, construction, and/or improvement of small homes, multifamily property, nonresidential property, and commercial or farm structures.

Cumulative GIF losses totaled approximately $1.34 billion on September 30, 1976, of which $77.5 million has been restored through appropriations. GIF received $42.5 million under the 1976 supplemental appropriation and $35 million under the 1977 appropriation.

COOPERATIVE MANAGEMENT HOUSING INSURANCE FUND

The Cooperative Management Housing Insurance Fund (CMHIF) was established on August 10, 1965, under authority of section 213 of the National Housing Act, as amended. Under CMHIF mortgages are insured which finance the purchase, construction, and/or rehabilitation of multifamily cooperative housing property. Also insured are supplementary loans which financed improvements and/or repairs of multifamily cooperative housing property or which provide funds for necessary community facilities.

Section 213(1) of the act authorized the:

--Establishment of a Participating Reserve Account and a General Surplus Account in CMHIF.

--FHA Commissioner to allocate the income or loss from operations in any semiannual period to either or both accounts.

--FHA Commissioner to distribute a share of the Participating Reserve Account to mortgagors as dividends after the CMHIF-insured mortgages have been paid and at such times before payment as he may determine. However, mortgagors have no vested rights in the account.

SPECIAL RISK INSURANCE FUND

The Special Risk Insurance Fund (SRIF) was established on August 1, 1968, under authority of section 238(b) of the National Housing Act, as amended. Under this fund mortgages are insured which finance (1) homes purchased by low-income families who are assisted with their mortgage payments by FHA, (2) homes purchased by low- and moderate-income families who, because of the nature of their credit histories or irregular income patterns, could not qualify for mortgage insurance under other FHA insurance programs, and (3) the repair, rehabilitation, construction, or purchase of property located in older, declining urban areas where conditions are such that eligibility requirements for mortgage insurance could not be satisfied under other FHA insurance programs.

Section 238(b) provides that SRIF be funded with a $5 million advance from GIF, to be repaid at such time and at such rates of interest the Secretary of HUD deems appropriate. The Housing and Urban Development Act of 1969 (12 U.S.C. 1715z-3(b)) authorized the Secretary to fund SRIF with advances from GIF in amounts that the Secretary determines necessary up to $20 million. As of September 30, 1976, $20 million had been advanced from GIF.

Cumulative SRIF losses on property sales totaled $723.3 million on September 30, 1976, and claims for mortgages covered under SRIF totaled $3.1 billion, but $200 million has been restored through appropriations. SRIF received $100 million under the 1976 supplemental appropriation and another $100 million under the 1977 appropriation.

PRINCIPAL HUD OFFICIALS

RESPONSIBLE FOR ADMINISTERING

ACTIVITIES DISCUSSED IN THIS REPORT

	Tenure of office	
	From	To
SECRETARY OF HOUSING AND URBAN DEVELOPMENT:		
Patricia R. Harris	Feb. 1977	Present
Carla A. Hills	Mar. 1975	Jan. 1977
James T. Lynn	Feb. 1973	Feb. 1975
George W. Romney	Jan. 1969	Feb. 1973
ASSISTANT SECRETARY FOR HOUSING-FEDERAL HOUSING COMMISSIONER (note a):		
Lawrence B. Simons	Mar. 1977	Present
John T. Howley (acting)	Dec. 1976	Mar. 1977
James L. Young	June 1976	Dec. 1976
ASSISTANT SECRETARY FOR HOUSING PRODUCTION AND MORTGAGE CREDIT-FHA COMMISSIONER (note a):		
David S. Cook	Aug. 1975	June 1976
David M. DeWilde (acting)	Nov. 1974	Aug. 1975
Sheldon B. Lubar	July 1973	Nov. 1974
Woodward Kingman (acting)	Jan. 1973	July 1973
Eugene A. Gulledge	Oct. 1969	Jan. 1973

a/On June 14, 1976, HUD combined the functions of the Assistant Secretary for Housing Production and Mortgage Credit-FHA Commissioner and the Assistant Secretary for Housing Management under a single Office of Assistant Secretary for Housing-Federal Housing Commissioner.

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