

UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548



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PROGRAM ANALYSIS
DIVISION

IN REPLY
REFER TO:

September 17, 1979

Dr. Delphis Goldberg ^{C.}
Subcommittee on Intergovernmental
Relations and Human Resources
Committee for Government
Operations
House of Representatives
Washington, D.C. 20515

HSE 1505

Dear Dr. Goldberg:

We thank you for the opportunity to respond to the Department of Housing and Urban Development (HUD) comments ~~(dated August 8, 1979)~~ on GAO testimony before your Subcommittee on May 23, 1979.

We find nothing in the HUD comments which warrants any modification to the thrust and particulars of our testimony. Although we agree with HUD comments concerning the desire of GAO and the Congress to have an effective Urban Development Action Grant (UDAG) program, we believe that HUD chose very selective and incomplete information to put in their comments. Furthermore, in contrast to the approach used in our testimony, HUD did not try to sketch a full picture of the many aspects of each grant.

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WHAT WE BASED OUR ANALYSIS ON

Contrary to HUD assertions, all available data known to exist at the time of our study was examined prior to the May 23 testimony. This includes final contracts, for those UDAG projects which had them, applications, press releases, and HUD analyses.

As indicated on page 3 of our testimony, our starting place was to examine the details of each grant at HUD's Washington Office. GAO staff then visited each of the UDAG site locations and HUD's regional offices to obtain the data necessary for our analysis.



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HUD alleges on page 2 of their comments that our methodology was based on incorrect assumptions. The conditions and scope of our study were stated in your letter of request, dated February 2, 1979, to the Comptroller General directing the "GAO analysis to include the following specific areas of investigation:

- the likely impact of these grants on the creation of permanent jobs within the local community.
- the extent to which grants are likely to yield future net public revenue for the local governments involved.
- the actual leverage or 'multiplier effect' of these grants in generating private investment within the community, taking into account other public investments made in the projects through the urban renewal and similar programs.
- who ultimately benefits from the UDAG program--the local community or private investors."

In our testimony to your Subcommittee, we stated that our analysis was limited to the economic impact of the 17 UDAG grants that we assessed.

We provided in our testimony to the Subcommittee an extensive discussion of the concept of leverage. In addition, we presented the following chart to help clarify some of the complex relationships which determine decisions to invest by the private sector of the economy and the role an UDAG could play in that decision.

In several UDAGs, our analysis indicated that the private business decision to invest was "levered" entirely by economic and business considerations and not to any significant degree to the award of an UDAG. In our judgment, what this means with respect to Chart 1 is that the private investment (PI) was already "levered" prior to an UDAG.

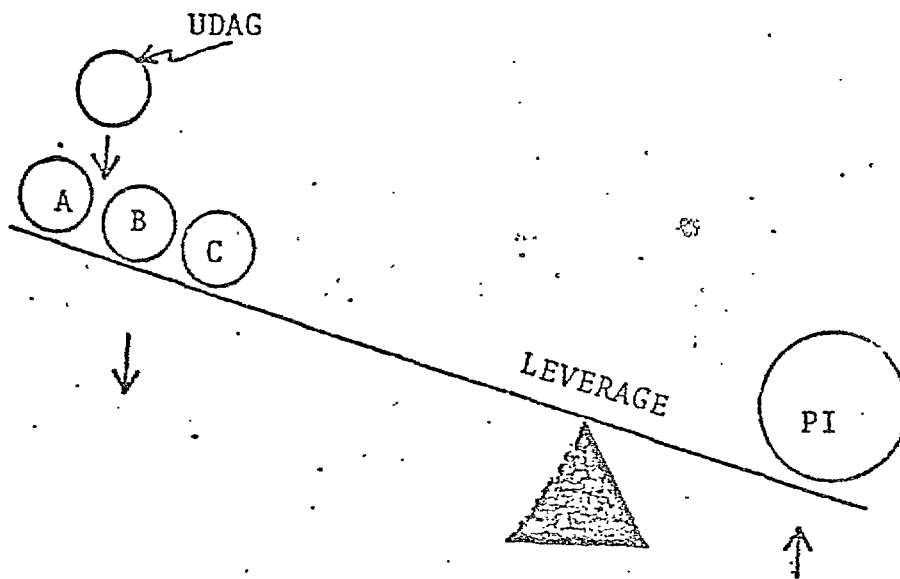
Concerning this matter of "leverage," the House of Representatives has passed an amendment to the Housing and Community Development Amendments of 1979 which prohibits the award of an UDAG in the absence of a determination of the Secretary of HUD that:

". . . such grant is necessary and essential to the initiation of the local development project for which it is to be used."

CHART 1

THE RELATIONSHIP BETWEEN UDAG
FUNDS AND PRIVATE INVESTMENT

Theory: The addition of an incremental weight (i.e., an UDAG) will lever private investment (PI).



▲ Overall Economic Climate, EG. Proximity to

- Market
- Resources

OTHER FACTORS WHICH
LEVER PRIVATE INVESTMENT

A -- Regulatory Considerations, EG. Environment

B -- Tax Considerations, EG. Abatements

C -- Provision of Infrastructure through other public investment

In a recent HUD publication, the leverage concept is mentioned and it appears that a high proportion of UDAGs have been made for projects which were already "levered" to some degree before an UDAG was awarded.

". . . 70.7 percent of the projects surveyed (123) have been planned prior to the enactment of the UDAG program." (See First Annual Report, UDAG Program, June 1979, p. 47.)

HUD mentions 11 criteria used in the selection of UDAGs and faults GAO for not addressing those criteria. Our intention, however, was not to examine the criteria HUD uses for selecting cities eligible for grants, but to assess the likely economic impact of the projects "levered" by these grants. In fact, we assumed that HUD used correct procedures in determining if a project was eligible for funding.

GAO METHODOLOGY IN REVIEWING 17 GRANTS

In our study of the 17 Urban Development Action Grants, we reviewed for each grant; the application, correspondence, press releases, and contract files at HUD Headquarters in Washington and each Area Office. All fully executed grant agreements at the time of our study (11 of the 17) were reviewed and considered in our analysis.

Contrary to HUD's assertion, GAO's analysis was not based on any misconceptions concerning operation of the Department. The comments of the Economic and Marketing Analysis Division (EMAD) of HUD's Area Office were not construed by us to represent the recommendation of HUD's Area Office or HUD itself. We did, however, consider these comments as inputs from knowledgeable, technical, and professional public servants. In every case where the comments of these professionals were used in our testimony, they were labelled appropriately as EMAD comments.

Again, the concern of our analysis was to look at the probable economic impact of a selected number of UDAGs--and not to assess the criteria for the selection of distressed cities that HUD suggests.

In performing our work, we used the most reliable, unbiased, and complete data. Although some disagreement could arise in judging where the weight of the evidence falls, we feel the difference in HUD's claims and GAO's analysis are not due to

such a judgment. It appears to us that HUD selectively used information in its response and did not present a complete picture of all the factors that affect a project. In contrast, we used the weight of the total evidence in making adjustments to the amount of private investment, taxes, permanent jobs, etc., leveraged by the UDAG projects reviewed.

Montezuma, Georgia

HUD's comments are based upon the contents of several pieces of correspondence which we reviewed, and this information was considered by us with all the other evidence available. These pieces of correspondence which HUD presents must be considered within the context of the entire chronology of events, site characteristics, and Area Economists' review comments.

The chronology of events presented in our testimony shows that the project was conceived years before the UDAG program was legislated by the Congress. In fact, the site was under option years before UDAG became law and the site purchased months before the UDAG award. The positive environmental site characteristics and the site's proximity to the plants raw materials (timber) and transportation facilities (two rail lines) strongly suggests that the UDAG portion of the project had little to do with the firm's decision. Furthermore, the company announced the beginning of actual construction before the UDAG was awarded.

Corning, New York

Again, nothing presented by HUD changes the facts or our conclusion. Corning, New York, agreed to make the public improvements months before the UDAG award. Our assessment indicates that a grant does not influence nor stimulate a commitment that is made before the application and award of the grant.

Concerning HUD's assessment that Corning was not able to fund the improvements, we did find that Corning, New York, has an AA bond rating, has used a small fraction of its available bonding, and will receive \$217,980 annually in additional property taxes from the project.

Cincinnati, Ohio

Since HUD admits it cannot identify investors who would locate on the 11 additional acres or would otherwise benefit

from the improvements, we fail to see how HUD can make claims with regard to jobs, private investment, and increased property taxes at this time. City officials explicitly stated that the new job estimate of 1,192 which we questioned was based on the total 59.4 acres, not the 11 acre portion involving the UDAG.

We do not agree that the UDAG provided the impetus for this project since it was conceived in the mid-1960's and has considerable other Federal monies involved in it. HUD's method of claiming all the new jobs, private investment, and increased tax base for the entire 59.4 acres project ignores completely the impact of the other Federal funds and efforts of local city officials involved in the project.

We have a similar concern with the claimed property tax increases of \$518,586. The increase is attributable to the total 59.4 acres in the redevelopment site, not just the 11 acre portion attributable to UDAG.

Baltimore, Maryland

Again, HUD comments do not warrant any change to our conclusion presented in the May 23, 1979, testimony. We did not include any indirect or spin-off effects in our analysis of UDAG projects since paragraph 570.457(e) of the UDAG regulations for selection criteria states:

"The private commitment must have a clear direct relationship to activities for which funding is being requested."

The UDAG funding was for the construction and initial operation of the hotel, not the retail and office space. We consider the retail and office space as indirect for several other reasons:

1. There are many other developments taking place in this area of Baltimore which impact, possibly as much or more than, the hotel.
 - a. Construction and completion of a 320,000 square foot C&P Telephone Company headquarters building in 1977. It is adjacent to the northside of the planned hotel.
 - b. Construction and completion in 1977 of a 32-story, 300,000 square foot World Trade Center by the Maryland Park Administration just east of the hotel site.

- c. Planned construction of a 250 unit apartment complex by Oxford Development Corporation south of the hotel site. Construction is scheduled to begin in late 1979.
 - d. Construction and completion in 1976 of a 106,000 square foot office building and 150-seat planetarium by the Maryland Academy of Sciences also south of the hotel site.
 - e. Construction of a \$15 million aquarium with a 300-seat auditorium east of the hotel site. Construction is scheduled for completion in late 1980.
 - f. Completion of the \$45 million Convention Center immediately west of the hotel site.
2. The developers of the office and retail space were involved in planning their respective developments prior to UDAG.
 3. The anticipated retail market relates to the convention market, not just a hotel market. The primary source of the convention market is the Convention Center.
 4. The HUD Area Economist also considered these activities as indirect.

To attribute the total private investment, jobs, taxes, etc., of the retail and office space fails to attribute appropriate leverage to the other relevant sources.

Further, even if indirect effects were considered in our analysis, we could not accept the job estimates of the developers other than the hotel. In one case 2,050 jobs are claimed as retained. This estimate of retained jobs is based on a formula of so many employees per square foot of space. We do not accept such an estimation method without first establishing:

1. That there is in fact tenants for the new building. We do not agree that available space automatically brings in tenants as this method indicates.
2. That the tenants in fact would leave the city without the new building.

We have similar concerns with the other job estimates.

Dayton, Ohio

We believe no modification to our analysis is warranted due to HUD's response. As stated previously, we did not include any indirect or spin-off effects of the UDAG projects according to paragraph 570.457(e) of the UDAG regulations for selection criteria.

HUD apparently takes exception to the difference between the \$12.9 million in private investment reported by HUD and the \$9.5 million in our analysis of the Dayton UDAG project. This difference is due to the renovation cost for an old post office building and the Daytonian Hotel. The UDAG funding was requested for the arcade, not the renovation of these two structures.

We consider these renovation activities as indirect for several other reasons as well:

1. They were not included in the original application.
2. The application itself classifies these activities as adjoining projects.
3. The HUD Area Economist in Columbus, Ohio, also considered these activities as indirect.
4. The renovation activities are outside those of the project developer, Arcade Square Ltd., and its partners--City of Dayton (general partner), the Mead Corporation, NCR Corporation, L.M. Berry Corp., E.F. MacDonald Corp., Dayco Corp., and Dayton Newspapers, Inc., (limited partners).

To attribute the total renovation costs of the post office and hotel solely to the UDAG fails to attribute leverage to other relevant sources. The Convention Center and the financial success of the architectural firm which is expanding into the old post office building have a substantial influence on the renovation activities. The other developments occurring in downtown Dayton, such as, the \$60 million Sinclair Community College, the new Federal building, the Convention Center Complex, the World Headquarters of Mead Corporation and the new publicly owned parking garages also impact upon these renovation activities.

HUD leaves the impression that the hotel developer's plans are totally contingent on the disposition of the UDAG grant. However, Dayton's application indicates the hotel developer

had purchased an option on the hotel one year prior to the UDAG application and had detailed renovation plans in-hand at the time of the application.

As stated in our testimony, the property tax estimates in the application include those from the renovation projects. Since these projects are indirect and Arcade Square, Ltd., received a 20 year tax abatement, no property taxes were attributed to the UDAG.

Troy, New York

GAO's analysis did divide the project into two parts, but not as described by HUD. Per our original testimony, the project was divided into a smaller shopping facility, which was committed prior to UDAG and included Denby's department store plus others, and a larger shopping facility which was contingent on the UDAG. These facts were obtained directly from the developer/owner, Mr. Carl Grimm.

HUD's selective use of information fails to bring out that while Denby's was in fact looking for a new location, it was looking for a place in downtown Troy. Further, a new location for Denby's was already provided for and committed in the developer's original concept for the mall.

We agree that the construction of the parking garage made it impossible for Denby's to stay in its old location, but the parking garage was being built to accommodate the expanded, larger mall concept which was being made possible by the UDAG. We do not agree in this case that the UDAG retained these jobs when the grant indirectly caused the displacement of the store in the first place. Besides, the relocation site for Denby's was already provided for in the original concept.

The differences in HUD's claims and GAO's analysis is the difference in the effects that would have been derived from the developer's original concept and that of the larger concept made possible by UDAG.

CONCLUSION

In conclusion, after a careful review of the HUD comments on our testimony of May 23, 1979, we reaffirm our position that there are a number of issues concerning UDAGs that should be addressed and researched in further detail. The basic issue is whether these Federal funds contribute to the economic development and vitality of "distressed cities." Investigating the extent to which UDAG's create permanent jobs, contribute to

future revenues of the distressed cities, and "leverage" private investment are aspects of the economic development issues that could shed some light on the degree of success of the UDAG program. HUD's claims of permanent jobs will not create those jobs--only a well-designed and well-administered program will accomplish those benefits expected by the Congress.

Sincerely yours, ,

A handwritten signature in cursive script, reading "Dennis J. Dugan", with a long horizontal flourish extending to the right.

Dennis J. Dugan
Chief Economist