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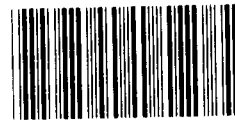
GAO

Report to the Chairman, Subcommittee on
Housing and Urban Development-
Independent Agencies, Committee on
Appropriations, U.S. Senate

April 1988

HOUSING PROGRAMS

Funding Approach for HUD's Section 8 Certificate Program Needs Changing



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Resources, Community, and
Economic Development Division

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April 18, 1988

The Honorable William Proxmire, Chairman
Subcommittee on Housing and Urban Development-
Independent Agencies
Committee on Appropriations
United States Senate

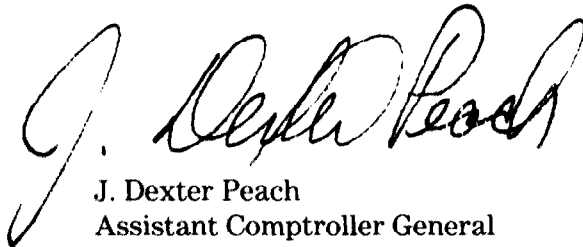
Dear Mr. Chairman:

In response to your September 9, 1987, request, this report provides information on the adequacy of the Department of Housing and Urban Development's (HUD) funding approach for its section 8 certificate rental assistance program.

As arranged with your office, we will distribute this report on the date of the Subcommittee's hearings on HUD's fiscal year 1989 budget request or 30 days from the date of this letter, whichever comes first. At that time, we will send copies to HUD, appropriate congressional committees and executive agencies, and the Director, Office of Management and Budget. Copies will also be sent to other parties upon request.

This work was done under the direction of John H. Luke, Associate Director. Major contributors are listed in appendix III.

Sincerely yours,



J. Dexter Peach
Assistant Comptroller General

Executive Summary

Purpose

In fiscal year 1987, the Department of Housing and Urban Development's (HUD) Section 8 Existing Rental Assistance Certificate Program provided assistance to enable about 800,000 low-income families to obtain decent, safe, and sanitary housing in private accommodations. Senator William Proxmire, Chairman, Subcommittee on HUD-Independent Agencies, Senate Committee on Appropriations, requested that GAO report on certain aspects of the section 8 program concerning

- whether it has sufficient budget authority and, if not, the potential shortfall;
- whether the fees paid to state and local public housing agencies (PHAS) to administer the program adequately compensate them for their costs; and
- how PHAS use administrative fees that exceed their actual costs.

Background

The section 8 rental certificate program provides subsidies for low-income families living in existing, private rental housing that meets HUD's quality standards. In requesting congressional funding authority, HUD estimates the total cost of the certificates on the basis of the total number of units to be funded, the 15-year period to be covered by the budget authority, and the most recent cost per unit.

HUD contracts with about 2,000 state and local PHAS across the country to administer the program. HUD provides these agencies with administrative fees, set by law, for making housing assistance payments to landlords on behalf of low-income families. The administrative funds are used to locate prospective families and landlords, certify family eligibility, and inspect housing units.

Results in Brief

HUD's budgeting approach underestimates the amount of funds needed over the 15-year budget authority period because it does not compute the cost of all factors having an impact on the program. As a result, many PHAS have depleted their originally authorized funding authority, and the Congress has had to provide supplemental authority totaling about \$1.3 billion between fiscal years 1982 and 1987. Moreover, any future units authorized under the program will likely require supplemental authority until HUD changes its funding approach to more accurately estimate total program costs.

Additionally, the 3-year administrative costs of the 70 PHAS that GAO sampled show that, although there are exceptions, most PHAS are reimbursed substantially more than their cost to administer the program, which results in a funding surplus. Because HUD allows PHAS wide discretion on how the surplus funds can be spent, PHAS use them for various purposes.

Principal Findings

Funding Approach Underestimates Costs

HUD's funding approach was designed to enable PHAS to offset program costs by drawing funds from project reserve accounts. The reserve accounts accumulate funding authority based on the average estimated first-year cost for each authorized unit projected over the 15-year budget authority period applicable to each certificate. However, HUD's funding approach does not consider all relevant factors. Omitted factors include the anticipated usage rate for rental certificates, expected tenant contributions to the rent, rent increases due to inflation over the 15-year period, and the amount of funding that PHAS receive from HUD to compensate them for their administrative expenses. Consequently, between fiscal years 1982 and 1987, the Congress has provided supplemental authority totaling over \$1.3 billion to pay for increases in rent and the administrative costs of PHAS.

It is likely that the need for supplemental funding authority will continue to increase in future years. In the earlier years of the section 8 program, PHAS used some of the budget authority for newly authorized certificates to offset the annual rent increases and administrative costs of older certificates. However, the need for supplemental authority is now much greater because fewer new rental assistance certificates have been added to the program in recent years and PHAS have had smaller amounts of budget authority from the newer certificates to offset the costs of the older ones.

GAO performed an analysis to compare HUD's approach for estimating total program costs with an alternative approach that considers all relevant cost factors. GAO's analysis assumed that 800,000 rental certificates were issued on the same day and each covered a 15-year period. This analysis, based on fiscal year 1987 cost data, shows that, when the relevant cost factors are considered, the total estimated program costs exceed the costs estimated under the HUD approach by \$2.1 billion to

\$11.8 billion, depending on the assumptions made about tenant contributions, rental increases, and administrative fees. If such additional costs were actually incurred, the rental certificate program would lose between 26,000 and 141,000 assisted housing units unless the Congress provided budget authority to meet them.

HUD agrees that its funding approach could result in substantial shortfalls but is reluctant to make changes until a decision is made on whether the rental assistance program will be replaced by a housing voucher program. The administration hopes to replace the certificate program with housing vouchers, but it is not certain if or when this will occur. Several studies are being performed, including a GAO review, comparing the cost, efficiency, and effectiveness of the certificate and voucher programs. HUD also believes it is difficult to accurately estimate costs over the 15-year budget authority period. While GAO agrees, it believes that HUD can provide the Congress with better cost information by estimating costs for each known factor and periodically updating this information to reflect actual costs.

Excess Administrative Fees

GAO analyzed rental certificate program administrative fees that HUD paid to 70 PHAS of various sizes, located throughout the country, for their 3 most recently completed fiscal years. GAO identified a net surplus of over \$22 million for the 3-year period, with a net surplus of about \$5.5 million in the most recent year for which data were available. The fee for this year was based on the lowest rate of reimbursement since the program was enacted.

Although GAO identified substantial differences between the administrative costs of PHAS and HUD's reimbursements, the results of GAO's sample are not projectable to the about 2,000 PHAS nationwide. HUD has awarded a contract to a consulting firm to study PHAS' administrative costs and plans to use the results of the study and this GAO review to determine an appropriate administrative fee.

HUD's guidance handbook states that PHAS may use the surplus administrative fee payments for "housing related purposes consistent with state and local law." However, HUD does not have guidelines specifying the type of expenditures that meet this criterion. GAO found that PHAS were using the funds for many different purposes, such as subsidizing other housing units, purchasing office space and equipment, and paying for office parties. In July 1987, HUD's Inspector General reported that HUD's policy regarding the use of surplus funds was vague and recommended

that HUD issue specific guidelines defining the use of the funds. GAO agrees with the Inspector General, but section 8 program officials said that HUD prefers to leave the primary responsibility for usage with the PHAS and has no plans to provide the PHAS additional guidance.

Recommendations

To provide the Congress with more accurate total program cost information for the section 8 certificate rental assistance program, GAO recommends that the Secretary of Housing and Urban Development develop budgeting procedures that compute and annually update costs, for existing and new certificates, based on all factors that have an impact on total program costs, including certificate usage rates, tenant contributions, rental increases, and administrative fees.

To provide a continuing basis for determining rates for section 8 rental certificate administrative reimbursements and for updating the amounts included for administrative fees in program cost estimates, GAO also recommends that the Secretary periodically determine the actual costs being incurred by PHAS throughout the country and provide this information to the Congress as part of HUD's annual budget request.

GAO also recommends that the Secretary issue more specific guidelines on the type of uses that are appropriate for surplus section 8 administrative fees.

Agency Comments

GAO discussed the information in this report with HUD officials and incorporated their comments where appropriate. However, as requested, GAO did not obtain official agency comments.

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Abbreviations

GAO	General Accounting Office
HUD	Department of Housing and Urban Development
PHA	public housing agency

Introduction

Section 8 of the Housing and Community Development Act of 1974 (Public Law 93-383) created the Existing Rental Assistance Certificate Program to provide rental assistance to low-income families.¹ The program, directed by the Department of Housing and Urban Development (HUD), is currently the principal means of providing federally subsidized housing to low-income families. The program is administered by some 2,000 state and local Public Housing Agencies (PHA) nationwide. The purpose of the program is to help lower income families in obtaining decent, safe, and sanitary housing in private accommodations. In fiscal year 1987, the federal government provided rental assistance certificates to about 800,000 low-income families.

How HUD Administers the Section 8 Existing Rental Assistance Program

HUD contracts with about 2,000 state and local public housing agencies across the United States to administer the section 8 existing program. PHAs certify families' eligibility for assistance, issue housing assistance certificates to eligible families, assist certificate holders in finding adequate housing units in the private market, inspect housing units to ensure that they meet HUD's housing quality standards, and make housing assistance payments to landlords on behalf of eligible families.

Eligibility for assistance under section 8 is generally limited to families with incomes that do not exceed 50 percent of the area's median income, adjusted for household size. Depending on income level, eligible families are required to pay up to 30 percent of their income after allowances for certain extraordinary expenses, such as high medical bills. Eligible individuals are given certificates that can be used to pay the owner of existing rental units the difference between the residents' payment and the normal rent, provided the normal rent does not exceed fair market value. The fair market rent, established by HUD for each local area, is intended to reflect the cost of modest rental housing available in the local private market.

How HUD Funds the Section 8 Existing Rental Program

The Congress annually approves new unit certificates and authorizes funds to HUD for each 15-year budget authority period. Since new certificates are added annually, in most cases PHAs have many certificates with different expiration dates. The 15-year budget authority assists PHAs in maintaining long-term stability in the operation of their rental assistance program. HUD's budget authority requests for these certificates are based on the average estimated first-year rent for all units

¹Section 8 of the 1974 act amended the United States Housing Act of 1937 (42 U.S.C. 1401).

nationwide. Therefore, the budget authority request per unit is the estimated average first-year rent per unit times 15. When HUD allocates housing assistance certificates to PHAS, it calculates the amount of funds PHAS need for the certificates by substituting the PHAS' local fair market rent in place of the average rent nationwide. HUD contracts with PHAS for three 5-year periods, which equates to the 15-year budget authority period.

To reimburse PHAS for their costs of administering the section 8 program, HUD pays PHAS

- a fee of 7.65 percent of the local two-bedroom fair market rent for each month a certificate is used to rent a unit;
- a one-time preliminary fee of up to \$250 for each newly authorized certificate to cover the cost of certifying families, assisting families to find housing units, and inspecting housing units; and
- a fee of \$45 to cover the cost of special assistance given to families with three or more minors to enable them to find suitable housing.

According to HUD regulations, if PHAS do not spend all of the amount received for administrative costs, they can use the excess for any "housing related purpose consistent with state and local law."

Objectives, Scope, and Methodology

On September 9, 1987, the Chairman, Subcommittee on HUD-Independent Agencies, Senate Committee on Appropriations, requested that we report to the Subcommittee on work we began earlier on the section 8 rental assistance program. We reviewed the program to determine

- whether it has sufficient budget authority and, if not, the potential shortfall;
- whether the fees paid to state and local PHAS to administer the program adequately compensate them for their costs; and
- how PHAS use administrative fees which exceed their actual costs.

To accomplish these objectives, we conducted audit work at HUD headquarters in Washington, D.C.; and at selected regional offices in Fort Worth, Texas; Philadelphia, Pennsylvania; and San Francisco, California; and at the Los Angeles, California, field office. At these locations, we obtained the opinions of HUD officials on the adequacy of total program funding and the formula for reimbursing PHAS' administrative costs. We also obtained their opinion on PHAS' expenditures of surplus administrative fees.

To obtain a national perspective on the program, we selected a sample of 70 PHAS in 9 of HUD's 10 regions. We categorized these PHAS on the basis of the number of section 8 existing units in their program. Our sample included PHAS in both metropolitan and nonmetropolitan areas. Our sample is not projectable to all of the more than about 2,000 PHAS nationwide because we did not review the approximately 250 PHAS that would have been required to obtain a statistically representative sample. (See app. II for detailed information about our sample PHAS.)

We collected and reviewed financial data for all 70 PHAS for their last 3 completed fiscal years. We made site visits to 45 PHAS, contacted 16 by telephone, and obtained the financial data for the remaining 9 at the HUD regional office. For those PHAS we visited or telephoned, we interviewed PHA officials to obtain their views on the adequacy of program funding, administrative fees, and the uses of surplus administrative fees. We also obtained documentation of the expenditures PHAS made through the use of surplus administrative fees. To determine whether the program has sufficient initial budget authority for the 15-year period, we made projections on funding requirements on the basis of (1) several scenarios based on our discussions with HUD officials and (2) consumer price and income data of the Bureau of Labor Statistics and the Bureau of the Census.

We made our review in accordance with generally accepted government auditing standards. Our review was made between August 1986 and December 1987.

HUD's Budgeting Approach Understates Housing Unit Costs, Resulting in Supplemental Funding Requirements

HUD's budget submissions do not provide the Congress with reasonably accurate estimates of full program costs over the 15-year budget authority period for section 8 rental housing certificates. The principal reason why this occurs is that HUD does not consider all cost elements at the time it submits the budget, such as rent increases and the fees that it will pay to PHAS for administering the program. As a result, HUD routinely underestimates the rental certificate program costs and, from fiscal year 1982 through fiscal year 1987, HUD has sought \$1.3 billion in supplemental budget authority to avoid a loss of assisted housing units under the rental certificate program.

In the future, it will likely be necessary for the Congress to provide even larger amounts in supplemental budget authority or lose assisted housing units under the rental certificate program. More funds will be needed because fewer certificates are being added to the program and PHAS will have smaller amounts of budget authority from new certificates to offset the costs of the older certificates. In this regard, in the early years of the program, PHAS used some of their budget authority for newly added certificates to offset increases due to inflation and the administrative costs related to older certificates. Since 1981, however, the number of new certificates added to the section 8 program has decreased substantially, and PHAS are less able to cover the increased costs of the older certificates with the budget authority provided for the new certificates.

The Congress needs the best information possible on total program costs to make informed decisions about assisted housing policies and funding levels. Even though it is difficult to precisely estimate costs for 15-year periods, we believe that HUD could provide the Congress with more accurate estimates by considering all factors having an impact on program costs.

HUD's Funding Approach Does Not Compute All Program Costs

When HUD estimates the total cost of section 8 rental certificate units, it bases its estimate on the total number of units to be funded, the period to be covered by the budget authority, and the most recent cost per unit. HUD does not, however, include estimates for other factors that have a significant impact on the 15-year costs of the rental certificate units. These factors include the anticipated percentage of the certificates that will be in use at any one time, the estimated amount that the tenants contribute to the rent, the rent increases due to inflation over the 15-year period, and the amount of funding the PHAS receive from HUD to cover their costs of administering the program.

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HUD allocates the budget authority it receives to individual PHAS located throughout the country. The budget authority allocation is based on the number of rental certificates that HUD has issued to the individual PHAS. On the basis of their allocations, the PHAS establish "reserve accounts" to fund the current- and future- year costs of the rental certificates. According to officials of HUD's Office of Financial Management, when the Congress provides HUD with 15-year budget authority for housing certificate units, HUD is allowed to make payments to PHAS based on this authority without the need to receive a specific additional appropriation for this purpose. That is, HUD makes annual payments to PHAS up to the amount of the budget authority they have been allocated for their rental certificates.

According to HUD officials representing the Office of Elderly and Assisted Housing, which is responsible for implementing the section 8 rental certificate program, HUD's approach for funding the program over the 15-year period does not totally disregard factors that will have an impact on the cost of the program; rather, HUD assumes that the factors will offset each other and thus does not compute the costs attributable to each factor. These officials told us that it is extremely difficult to provide an accurate estimate of the total budget authority that would be required over the 15-year period because of the variability of the factors involved. While we agree it is difficult to precisely estimate costs for 15 years, HUD can provide estimates that better approximate total costs. To do this, HUD can use readily available data, as discussed below, to estimate the total costs attributable to each factor and then periodically update these estimates based on actual costs.

The HUD officials also told us that, in preparing its budget estimates, HUD realized that the budget authority requested would not be adequate to fund the rental certificate units over the 15-year budget authority period. HUD believed, however, that the budget authority would be adequate for at least 5 to 7 years and that, if the funding became depleted at individual PHAS, it would request that the Congress amend the 15-year budget authority amount to meet the shortfalls. As discussed later, HUD has requested such amendments on several occasions. However, this budget and amendment process does not provide accurate estimates of total program costs for the Congress when it is making decisions about funding levels for various housing programs.

Even though HUD recognizes that its funding approach does not compute all program costs and, consequently, does not provide the Congress with an accurate estimate of full program costs, HUD does not intend to revise

its approach, pending the outcome of congressional and executive branch deliberations on whether the rental certificate program will continue or be replaced by the housing voucher program proposed by the administration. The administration hopes to replace the section 8 certificate program with vouchers, but it is not certain if or when this will occur. Meanwhile, certificates are still being budgeted and used. The voucher program, which is similar to the section 8 certificate program, is intended to provide assisted families with a greater choice in the selection of a rental unit. The voucher program permits families to rent units for costs below or above the fair market rent in the local geographic area. Monthly assistance payments are based on the differences between a payment standard for the area and 30 percent of the families' monthly net income.

Several studies are being performed, including a GAO review, comparing the cost, efficiency, and effectiveness of these programs. The current deliberations concerning the future of these programs demonstrates the importance of the Congress' being accurately informed of the programs' total cost. Likewise, until a decision is reached on the future of rental certificates, it is important for HUD to consider all cost factors in estimating the costs of the rental certificate program because each fiscal year's budget authorization for rental certificates otherwise would likely require future increases in budget authority.

Comparison of HUD Assumptions and Actual Circumstances

As part of our analysis, we obtained data on each program cost factor and compared the data with the assumptions that HUD makes when it requests budget authority for the section 8 rental certificate program. Data for this analysis were readily available from HUD records and the Consumer Price Index.¹ Table 2.1 compares the HUD assumptions with actual circumstances and is followed by a discussion of each cost factor.

Table 2.1: Comparison of HUD Assumptions and Actual Circumstances

Cost factor	HUD assumption	Actual circumstance
Certificate usage	100 percent	93.7 percent
Tenant contributions	None	30 percent of adjusted income
Rent increases	None	Based on inflation
Administrative fees	None	7.65 percent of the two-bedroom fair market rent

¹A measure of the average price change of various goods and services customarily purchased by urban consumers. The Consumer Price Index is published monthly by the Bureau of Labor Statistics, Department of Labor, and is commonly called "the cost of living index."

Certificate Usage

As shown in table 2.1, HUD's funding approach assumes that PHAS will have a 100-percent rate of certificate usage, but the actual rate is lower. As of March 31, 1987, the latest date for which information is available, the average usage rate for section 8 rental certificates throughout the country was 93.7 percent, the same rate reported by the PHAS included in our sample. The difference between the level HUD assumed and the actual level results in a surplus in the section 8 reserve accounts, which is used by PHAS to partially pay for future rent increases.

Tenant Contributions

Although HUD does not include any tenant contributions in its funding approach at the time of budget submission, most tenants pay 30 percent of their adjusted income toward their rent. The following is an illustration. HUD provides \$500 to a PHA for a unit that rents for \$500. However, if such a unit were occupied by a renter having an income of \$1,000 per month, the renter would pay \$300 (30 percent of income) and the PHA would pay the remaining \$200. The difference between the amount HUD provides and the amount the PHA paid, or \$300 in this case, is maintained by the PHA in a reserve account and is used to pay future rent increases.

Rent Increases

Although reserve account surpluses result from HUD's treatment of certificate usage rate and tenant contributions, deficits result from HUD's not considering the impact of rent increases caused by inflation. HUD's funding approach assumes that rents will remain constant over the budget authority period. Nonetheless, the actual rent increases paid by HUD are significant. In this regard, HUD uses the residential rent and the fuel and utilities components of the Consumer Price Index to develop inflation factors for (1) updating fair market rents for new units and (2) serving as annual adjustment factors for existing section 8 units. From October 1979 to April 1987, HUD's fair market rent for an average two-bedroom unit increased by over 70 percent. Because such inflation increases are not estimated in HUD's funding approach, they result in funding shortfalls.

Administrative Fees

As shown in table 2.1, administrative fees paid to PHAS are not considered in HUD's approach. During each year of the section 8 program, however, the PHAS have received such a fee. During fiscal year 1987, for example, PHAS received an administrative fee of 7.65 percent of the local two-bedroom fair market rent for each month a unit was under lease—a significant amount of money. For example, a PHA having 1,000 units

with a two bedroom fair market rent of \$500 and an occupancy rate of 95 percent would receive an administrative fee for the year totalling \$436,050. The PHAS also receive a one-time fee of up to \$250 for each new unit that is leased and a special \$45 fee for hard-to-house families.

HUD obtains the funds necessary to pay administrative fees from the budget authority for the section 8 program. In effect, the fees are reductions from the total amount of the budget authority available to fund rental units. Because the fees are not factored into HUD's budgeting approach, they result in deficiencies in funding needed to pay rental certificate costs.

Significant Funding Shortfalls Are Likely

Because HUD did not consider all program cost factors when it requested funds from the Congress for the section 8 rental certificate program, many PHAS have depleted their project reserves, as HUD originally anticipated might happen. Moreover, future rent increases and administrative fees that have not been provided for in the budget authority may exceed overall project reserves by billions of dollars.

When a PHA depletes its project reserve, HUD requests from the Congress an amendment to its budget authority to keep the PHA's section 8 rental assistance program viable. If the Congress did not provide this amendment funding authority, the PHAS would face a loss of assisted housing units because they would no longer be able to provide section 8 housing funds to assist low-income families in paying their rent.

Twelve of the PHAS in our sample of 70 have been provided a total of \$6.1 million in amendment authority since the beginning of their programs to avoid a loss of assisted housing units. As shown in table 2.2, HUD has allocated about \$1.3 billion in amendment budget authority nationwide from fiscal year 1982 through 1987 to PHAS that have experienced shortfalls. We were unable to determine the amount of amendments prior to 1982 because HUD did not keep separate records of amendments for the various section 8 programs before that time. That is, the amendments for the new construction, the substantial and moderate rehabilitation, and the housing certificate programs were included as one budget item.

Chapter 2
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**Table 2.2: Section 8 Rental Certificate
 Budget Authority, Fiscal Years 1982-87**

Fiscal year	Amendment budget authority
1982	\$63,073,034
1983	196,173,281
1984	33,647,416
1985	178,669,881
1986	419,395,680
1987	422,171,872
Total	\$1,313,131,164

As table 2.2 indicates, the need for amendment budget authority has increased substantially during the last 2 fiscal years. More amendments have been needed during this period because fewer new units have been added to the program. As explained earlier, PHAs use their budget authority for new units to offset increases in costs for older units, and PHAs have had smaller amounts of budget authority with which to do this in recent years because of the reduction in rental certificates. The number of certificates added to the program has decreased steadily in the past several years from a high of 140,180 certificates in fiscal year 1981 to a low of 9,497 certificates in fiscal year 1987.

In a June 12, 1987, letter to the Secretary of HUD, the Chairman, Subcommittee on Housing and Community Development, House Committee on Banking, Finance and Urban Affairs, expressed his concern about the potential shortfalls under the program. On the basis of his request, as of April 1988, HUD was developing an estimate of the total future shortfall for the 800,000 units in the program through their various expiration dates.

Because this information was not available, we performed an analysis to compare the total costs of the program as estimated both under HUD's approach and under an alternative approach that considers all cost factors—rental certificate usage rates, tenant contributions, rental increases, and administrative fees. In our analysis, we assumed that all 800,000 existing certificates were issued on the same day and projected the cost over a 15-year period. Using HUD's approach, we projected program costs by multiplying the 800,000 certificate units by the average fair market rent for 1987 and then multiplying this amount by 15 years. In contrast, under the alternative approach, we assumed a 95-percent rental certificate usage rate and used various assumptions, explained

below, regarding tenant contributions, rent increases, and administrative fees. We assumed a 95-percent occupancy rate for all of our estimates because HUD expects PHAS to maintain approximately that level. We assumed that rents and PHAS' administrative costs would increase by either 5 or 6 percent each year and that tenant contributions would increase at rates of 2 to 5 percent each year. These assumptions were based on our discussions with HUD officials and on consumer price and income data of the Bureau of Labor Statistics and the Bureau of the Census.

Our analysis using the two estimating approaches shows that, when all cost factors are considered, the total estimated program costs exceed the costs estimated under the HUD approach by \$2.1 billion to \$11.8 billion, depending on the specific assumptions, discussed above, that are used. If such costs were incurred, the rental certificate program would lose between 26,000 and 141,000 assisted housing units unless the Congress provided additional budget authority to meet the additional costs.

Conclusions

In making its housing program decisions, the Congress should be able to rely on HUD to provide reasonably accurate total program cost information for the 15-year period covered by the section 8 rental certificate program. HUD's funding procedure does not provide such information because it does not consider all of the cost elements that will have an impact on the total program costs. Because HUD's funding approach has resulted in funding shortfalls, HUD has requested, and the Congress has provided, about \$1.3 billion in budget authority from fiscal year 1982 through 1987 to supplement the initial budget authority provided to PHAS. Additional amounts of supplemental budget authority for existing rental certificate units could amount to billions of dollars, and each fiscal year's budget authorization for new rental certificates will be subject to such increases unless HUD changes its funding approach to more accurately estimate the total costs of the program.

Although many uncertainties make it difficult to precisely estimate future costs, we believe that HUD can provide more accurate estimates by using available data to directly consider all of the factors that comprise total costs of the rental assistance program. This could be done in HUD's initial budget request, as well as in periodic updates reflecting actual costs and revisions to the estimated budget authority, to provide the Congress with better total cost estimates for making comparisons of the various alternatives available for providing assisted housing.

**Recommendation to
the Secretary of
Housing and Urban
Development**

To provide the Congress with more accurate total program cost information for the 15-year budget authority of the section 8 certificate rental assistance program, we recommend that the Secretary of Housing and Urban Development develop budgeting procedures that compute and annually update costs, for existing and new certificates, based on all factors that have an impact on total program costs, including certificate usage rates, tenant contributions, rental increases, and administrative fees.

HUD Payments to Public Housing Agencies Exceed Program Administrative Expenses

HUD regulations authorize payments from section 8 funds to compensate PHAS for their administrative costs of operating the housing certificate program. These administrative fees often result in surpluses not needed by the PHAS for administrative expenses. PHAS have accumulated and placed these surpluses in reserve accounts, but section 8 legislation does not address the surpluses or how they are to be spent. However, under its section 8 guidance handbook to PHAS, HUD allows the PHAS to use these funds for any "housing related purpose consistent with state and local law."

When it reported the Housing and Community Development Act of 1987 (Public Law 100-242, 101 Stat 1815, dated February 5, 1988), the conference committee asked us to perform a review of this area. In our sample of 70 PHAS, we found that in the PHA's most recently completed fiscal year net surplus administrative fees totaled about \$5.5 million. Based on the last three available financial reports for these PHAS covering their last 3 completed fiscal years, surpluses totaled over \$22 million. Although our sample results are not statistically projectable to the more than about 2,000 PHAS administering the rental certificate program nationwide, they demonstrate the potential for substantial differences between annual administrative costs and reimbursements received by PHAS throughout the country.

Currently, PHAS' administrative fees are based on a set percentage rate per unit rented rather than on the amount of the payment that would be needed to meet administrative costs. HUD has awarded a contract to a consulting firm, however, to study and make recommendations regarding the appropriate amount of the administrative fee. HUD told us the study will be completed in April 1988 and it hoped to present this information to the Congress to help it in its deliberations on future administrative fees.

The PHAS in our sample which had surplus administrative funds used the surpluses for varying purposes. Some used the funds for the section 8 housing program; others used them for other federal or state programs such as HUD's public housing modernization program. Still others used the funds for buying computers or making office renovations. A few PHAS told us that they were reluctant to use the funds because they were uncertain of how they should be used.

In July 1987, HUD's Office of Inspector General reported that HUD's policy regarding the use of surplus funds is vague and recommended that HUD issue specific guidelines defining the appropriate use of the funds.

HUD officials said, however, that HUD prefers to leave the primary responsibility for the use of the funds with the PHAS.

The Basis for HUD's Administrative Fee

The section 8 authorizing legislation [42 U.S.C. 1437 f(b)(1)] permits HUD to enter into Annual Contributions Contracts with PHAS to help fund PHAS' activities. The standard Annual Contributions Contract provides for PHAS to receive a reasonable fee from HUD to reimburse them for the costs they incur in administering the program. Administrative costs covered by the fee include making payments to housing owners, reexamining the income of the family holding the certificate, providing housing information and assistance to low-income families, reinspecting leased units, and receiving new families into the program to replace those who leave. Administrative overhead costs are also intended to be covered by the administrative fee.

HUD officials in the Office of Elderly and Assisted Housing told us that when HUD implemented the section 8 certificate program in 1974, it decided to provide PHAS with an ongoing administrative fee of 8.5 percent of the local two-bedroom fair market rent established by HUD for each month a unit is under lease. They told us that the 8.5 percent was based on the costs of administering other HUD housing programs as well as estimates of what HUD thought it would cost PHAS to administer the section 8 certificate program. The HUD officials also told us that 8.5 percent was the fee percentage that property management companies usually received for managing housing units at that time. HUD officials told us that HUD reduced the fee to 7.65 percent in 1985 in response to the Office of Management and Budget's request for an overall reduction of 10 percent in HUD spending.

The Housing and Community Development Act of 1987 provided an expressed statutory basis for the administrative fee and increased the administrative fee to 8.2 percent. In addition, the act authorized HUD to pay for unexpected, extraordinary PHA costs approved by the Secretary of Housing and Urban Development. The Conference Report requested that we perform this review and report our findings by June 1988 for further congressional deliberation on the appropriateness of the administrative fee rate.

Most Sampled PHAs Profited Under HUD's Administrative Fee Rate

To determine the adequacy of HUD's administrative fee payments to meet PHA expenses, we selected 70 PHAs located throughout the nation. Our sample included PHAs of various sizes located in both metropolitan and rural areas. We obtained information from the PHAs on the amount of administrative fees they received, their expenses, and their administrative account surpluses or deficits for their last 3 completed fiscal years.

The first 2 years of our sample data reflect an administrative fee of 8.5 percent. The most recent year reflects a 7.65 percent rate. The average for the 3-year period is 8.2 percent, which is the rate currently set by law.

Our work showed that the PHAs had an overall net surplus of over \$22 million. About \$5.5 million of the surplus occurred during the PHAs' most recently completed fiscal year, during which time the administrative fee was 7.65 percent—the lowest rate it has been since the program was enacted. Although our sample results are not statistically projectable to the more than about 2,000 PHAs administering the rental certificate program nationwide, they demonstrate the potential for substantial differences between annual administrative costs and reimbursements received by PHAs throughout the country.

Figure 3.1 summarizes the information we obtained on the PHAs' total net surpluses and deficits for the 3 years sampled. As figure 3.1 shows, 60 of the 70 (or 86 percent) had surpluses. The average surplus was \$381,521, and the average deficit was \$56,880.

Chapter 3
 HUD Payments to Public Housing Agencies
 Exceed Program Administrative Expenses

Figure 3.1: Number of PHAs With Various Ranges of Surpluses and Deficits Over 3-Year Period Sampled

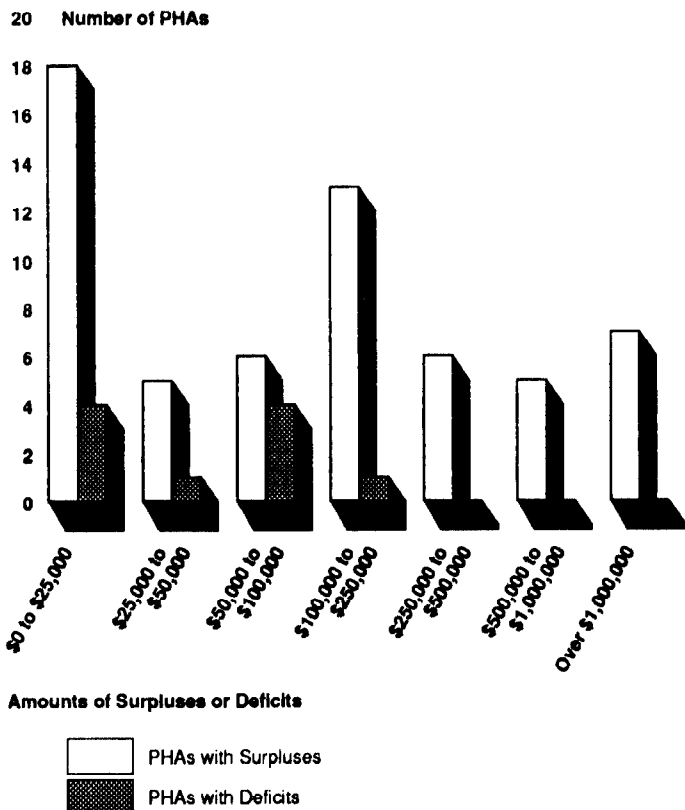


Table 3.1 shows that 51, or 73 percent, of the PHAs sampled also had surpluses during the most recent year sampled when the lowest administrative fee rate (7.65 percent) was in effect.

Table 3.1: Number of PHAs Sampled With Various Ranges of Surpluses or Deficits for Last Year Sampled

Amount of surplus or deficit	Number of PHAs with surplus	Number of PHAs with deficit
\$0 to \$50,000	30	18
\$50,000 to \$100,000	7	0
\$100,000 to \$250,000	4	0
\$250,000 to \$500,000	6	1
Over \$500,000	4	0
Total	51	19

As shown in table 3.1, only one PHA had a deficit of over \$50,000. The amount of this deficit, about \$417,000, represented about 62 percent of the total deficit of the 19 PHAs that reported a deficit for the year. PHA

officials told us that the deficit resulted primarily from an unusually large number of lawsuits by section 8 tenants and PHA vendors.

In reviewing the surpluses and deficits, we also considered the size of PHAs and their geographic location. In this regard, in enacting the Housing and Community Development Act of 1987, the Congress provided for HUD to increase the administrative fee beyond the 8.2-percent level to compensate PHAs for potentially higher costs of administering small programs and programs covering large geographic areas. However, we found that most had surpluses regardless of the PHAs' size or geographical location. Appendix II shows our sample results by PHA location and the amount of surplus or deficit for the 3-year period. Table 3.2 summarizes the net surpluses and deficits according to the size of the PHAs for the 3-year period sampled.

Table 3.2: Total Surpluses and Deficits for 3-Year Period by PHA Size

Number of units	Total surpluses	Total deficits
1-149	\$270,687	\$1,729
150-499	1,373,113	106,996
500-999	1,390,345	225,065
1,000 or more	19,857,132	235,010
Total	\$22,891,277	\$568,800

In discussing our data with HUD officials in the Office of Elderly and Assisted Housing, we were told that HUD believes the administrative fee payments, even at the 7.65-percent level, probably result in surplus payments to most PHAs and that the level of payment should be reduced. These officials said that HUD has contracted with a consultant to conduct a study of PHAs' actual administrative costs. This study is scheduled to be completed in April 1988. According to the HUD officials, they intend to use the consultant's study and the results of our review to determine the appropriate administrative fee that should be paid to PHAs.

PHAs Are Using Surplus Funds for Various Purposes

Section 8 legislation does not address the use of surplus administrative fees. Chapter 8-2, paragraph d of HUD Handbook 7420.7 provides that surplus administrative funds shall be used for any "housing related purpose consistent with state or local law."

We noted during our review that HUD's Office of Inspector General has recommended that HUD issue more specific guidelines on the PHAs' use of section 8 surplus administrative funds. In this regard, in April 1987, the

HUD Office of Inspector General questioned a PHA's expenditures from surplus section 8 administrative fees. For instance, in conjunction with its 50th anniversary celebration, the PHA used \$76,000 in surplus administrative fees, partly to buy band equipment and pay for travel expenses for a drum and bugle corps to represent the PHA at various parades and other festivities. It also paid for a lobbyist to defeat a legislative effort to increase the number of the PHA's commissioners.

In July 1987, HUD's Office of General Counsel responded to the Inspector General's concerns. It stated that there is very minimal governance in HUD legislation, regulations, or handbooks regarding the use of surplus section 8 administrative fees. The Office of General Counsel concluded, therefore, that PHAs are afforded broad authority for expenditures of such fees and that the expenditures were legal.

In response to the HUD General Counsel's opinion, the Inspector General stated that HUD's policy concerning the use of section 8 surplus administrative fees is vague and nonspecific and that it is unclear what constitutes a "housing related" purpose. According to the Inspector General, under HUD's policy, many obscure and questionable activities can be justified, giving the impression that PHAs are wasting, for frivolous or improper activities, funds that could be used to better the living conditions of low-income housing residents.

We believe HUD has the authority to provide PHAs more specific guidance on how surplus administrative funds should be used. Further, we agree with the HUD Inspector General that HUD's criteria are vague. During our review, we found that section 8 surplus administrative fees were used for many different purposes. Some of the uses we noted included purchasing computers to help administer the section 8 program; buying automobiles used in connection with performing housing inspections; subsidizing the costs of additional low-income housing units; purchasing PHA office furniture, softball uniforms, and birthday cards for PHA employees; modernizing PHA housing units; purchasing office space for PHA employees; paying for PHA holiday parties; and purchasing exercise equipment for PHA employees. A few PHAs told us they have not used the funds because they are uncertain of how they should be used and would like guidance from HUD.

We discussed the results of our work and the status of the Office of Inspector General's recommendations with the HUD official in charge of the section 8 certificate program. According to that official, HUD prefers to leave the primary responsibility for the use of the funds with the

PHAS in view of the General Counsel's conclusion on the broad authority afforded to the PHAS for the expenditure of these funds. He did state, however, that HUD is proposing a change in its section 8 housing certificate handbook requiring PHAS to notify HUD 10 days in advance of withdrawing surplus funds. The purpose of this change is not to require HUD's approval of the specific use of the funds. Rather, HUD will use this information to ensure that the PHAS are adequately administering the section 8 program before any excess fees are spent for other purposes.

Conclusions

We found that the fees HUD paid to most of the PHAS within our sample substantially exceeded the costs of administering the section 8 rental certificate program. Even though we examined only 70 of the more than about 2,000 PHAS involved in the section 8 program throughout the country, we identified a net surplus of over \$22 million for the 3-year period we reviewed. We believe that the Congress periodically needs information on the actual costs being incurred by PHAS throughout the country. With this information, the Congress would have an improved basis for its deliberations on the fee that should be paid PHAS as reimbursement for their administrative costs.


HUD guidance gives PHAS wide discretion on how surplus administrative fees will be spent. The HUD Inspector General has recommended that more specific guidance be established to ensure the prudent use of PHAS' surplus funds, but cognizant HUD officials prefer to allow PHAS wide discretion in the use of the funds. We agree with the Inspector General and believe the Secretary of HUD needs to clearly define how the funds should be used.

Recommendations to the Secretary of Housing and Urban Development

To provide a continuing basis for determining rates for section 8 rental certificate administrative reimbursements and for updating the amounts included for administrative fees in program cost estimates, we recommend that the Secretary of Housing and Urban Development periodically determine the actual costs being incurred by PHAS throughout the country and provide this information to the Congress as part of HUD's annual budget request.

We also recommend that the Secretary issue more specific guidelines on the type of uses that are appropriate for surplus section 8 administrative fees.

Request Letter

JOHN C. STENNIS, MISSISSIPPI, CHAIRMAN		
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FRANCIS J. SULLIVAN, STAFF DIRECTOR J. EDITH LEAHY, MINORITY STAFF DIRECTOR		
September 9, 1987		
The Honorable Charles A. Bowsher Comptroller General of the United States U.S. General Accounting Office 441 G Street, N.W. Washington, D.C. 20548		
Dear Mr. Bowsher:		
<p>On August 26, 1987, members of your office briefed Mr. Tom van der Voort, Staff Director of the Subcommittee on HUD-Independent Agencies, Senate Appropriations Committee, on your review of public housing agency operating and administrative reserve accounts for the Department of Housing and Urban Development's (HUD's) Section 8 existing program.</p>		
<p>I am very much interested in your work because the preliminary results seem to indicate that HUD's program funding formula for operating reserves does not adequately estimate costs over the 15 year period the reserves are meant to cover. As a result we may soon be having a very large shortfall in program funding for rent subsidies. Despite this potential shortfall in operating reserves, your preliminary results apparently show that for administrative expenses the majority of public housing agencies are reimbursed by HUD for more than the cost they incur to administer the program and have accumulated significant amounts of excess dollars. Furthermore, HUD appears to be allowing public housing agencies to use these funds for any housing-related purpose rather than to help offset the operating reserve shortfall.</p>		
<p>Because the above issues directly affect HUD's appropriations, I am requesting that GAO issue a report to the Subcommittee in time for your findings, conclusions and recommendations to be used when the Subcommittee considers HUD's fiscal year 1989 budget request. Please contact Mr. van der Voort to coordinate the timing of your report.</p>		
Sincerely,  William Proxmire Chairman HUD-Independent Agencies Subcommittee		

Sampled PHAs' Surpluses and Deficits for 3-Year Period by HUD Regional Office^a

Region and PHA	Number of units under contract	Surplus or (deficit)			Net for 3-year period
		First year	Second year	Third year	
I. Boston:					
Augusta, Mass.	57	\$6,488	\$6,809	\$8,932	\$22,229
Manchester, N.H.	783	31,645	36,374	2,417	70,436
Boston, Mass.	4,355	277,680	103,561	649,346	1,030,587
Cambridge, Mass.	869	37,531	(37,940)	(24,021)	(24,430)
Quincy, Mass.	655	(28,857)	1,327	(32,500)	(60,030)
Total	6,719	324,487	110,131	604,174	1,038,792
III. Philadelphia:					
Mifflin Co., Pa.	115	6,577	19,712	17,311	43,600
Montour Co., Pa.	49	460	1,437	827	2,724
Bucks Co., Pa.	1,362	112,429	172,790	102,348	387,567
New Castle Co., Pa.	1,090	(82,964)	62,688	31,735	11,459
Philadelphia, Pa.	6,217	(237,674)	783,273	268,699	814,298
Virginia Housing Development Authority	4,879	302,605	187,117	10,128	499,850
Nanticoke, Pa.	51	3,895	1,354	(2,132)	3,117
Total	13,763	105,328	1,228,371	428,916	1,762,615
IV. Atlanta:					
Marietta City, Ga.	300	58,216	55,001	42,703	155,920
East Point, Ga.	226	3,689	12,866	(2,427)	14,128
Fort Lauderdale, Fla.	434	7,309	(15,759)	(48,087)	(56,537)
Marietta Co., Ga.	531	(14,466)	(14,466)	(19,254)	(48,186)
Atlanta, Ga.	4,033	122,785	228,747	(417,590)	(66,058)
Georgia Residential Finance Agency	5,853	342,557	324,939	(14,758)	652,738
Total	11,377	520,090	591,328	(459,413)	652,005
V. Chicago:					
Southfield, Mich.	100	2,812	19,734	0	22,546
Waukegan, Ill.	262	66,201	44,686	52,268	163,155
Bloomington, Ind.	583	15,127	(4,336)	1,840	12,631
Chicago, Ill.	9,326	962,588	270,122	900,400	2,133,110
Peru, Ind.	50	5,047	4,369	(312)	9,104
Total	10,321	1,051,775	334,575	954,196	2,340,546
VI. Fort Worth:					
McKinney, Tex.	130	2,364	6,954	13,189	22,507
Plano, Tex.	100	12,799	12,324	13,984	39,107
Garland, Tex.	303	12,978	26,210	1,349	40,537

(continued)

**Appendix II
Sampled PHAs' Surpluses and Deficits for
3-Year Period by HUD Regional Office^a**

Region and PHA	Number of units under contract	Surplus or (deficit)			Net for 3-year period
		First year	Second year	Third year	
Greenville, Tex.	203	(5,652)	2,500	879	(2,273)
Weatherford, Tex.	292	24,997	13,752	16,226	54,975
Denton, Tex.	566	34,475	58,201	7,099	99,775
Waco, Tex.	941	62,712	47,607	52,339	162,658
Austin, Tex.	1,348	(79,448)	99,504	133,495	153,551
Dallas, Tex.	3,600	182,177	(17,147)	125,417	290,447
San Antonio, Tex.	5,772	1,388,952	1,574,839	362,250	3,326,041
Fort Worth, Tex.	1,598	(32,757)	(108,471)	(13,117)	(154,345)
Total	14,853	1,603,597	1,716,273	713,110	4,032,980
VII. Kansas City:					
Cedar Rapids, Iowa	699	41,633	26,311	11,378	79,322
Kansas City, Kans.	626	65,712	87,733	49,866	203,311
St. Joseph, Mo.	587	51,835	48,892	56,085	156,812
Lincoln, Neb.	2,015	309,784	350,981	346,543	1,007,308
Manhattan, Kans.	90	668	1,512	(2,001)	179
Marshall, Mo.	103	7,258	7,404	(8,289)	6,373
West Plains, Mo.	111	521	7,253	2,941	10,715
Total	4,231	477,411	530,086	456,523	1,464,020
VIII. Denver:					
Stark Co., N.D.	145	11,825	11,344	2,293	25,462
Denver, Colo.	985	117,284	100,932	44,901	263,117
Pueblo, Colo.	640	65,167	65,087	57,517	187,771
State of South Dakota	1,741	98,053	152,782	91,820	342,655
Fountain, Colo.	125	15,779	6,798	(24,306)	(1,729)
Colorado Springs, Colo.	533	38,976	(9,649)	(5,149)	24,178
Salt Lake City, Utah	644	16,906	38,940	(13,611)	42,235
Total	4,813	363,990	366,234	153,465	883,689
IX. San Francisco:					
Burbank, Calif.	483	33,364	122,170	70,889	226,423
Redondo Beach, Calif.	479	20,764	59,155	111	80,030
Torrance, Calif.	403	0	31,694	22,391	54,085
Glendale, Calif.	573	93,589	141,892	93,856	329,337
Inglewood, Calif.	695	77,840	65,213	0	143,053
Anaheim, Calif.	2,127	^b	493,418	319,072	812,490
Long Beach, Calif.	3,077	249,797	449,159	214,297	913,253
Los Angeles, Calif.	18,347	536,351	(586,648)	35,690	(14,607)
Los Angeles Co., Calif.	2,150	295,491	341,875	153,405	790,771

(continued)

**Appendix II
Sampled PHAs' Surpluses and Deficits for
3-Year Period by HUD Regional Office^a**

Region and PHA	Number of units under contract	Surplus or (deficit)			Net for 3-year period
		First year	Second year	Third year	
Orange Co. Calif.	5,174	850,975	1,229,366	1,021,100	3,101,441
Riverside Co. Calif.	4,169	561,999	753,158	294,579	1,609,736
San Bernardino, Calif.	2,927	599,465	592,016	374,587	1,566,068
Santa Barbara, Calif.	855	(11,353)	(6,269)	(13,324)	(30,946)
Total	41,566	3,308,282	3,686,199	2,586,653	9,581,134
X. Seattle:					
Kennewick, Wash.	150	6,321	13,288	3,538	23,147
Pasco, Wash.	61	(640)	760	590	710
Renton, Wash.	104	(161)	3,624	6,844	10,307
Richland, Wash.	54	952	10,290	5,067	16,309
Everett, Wash.	547	72,378	78,259	37,473	188,110
Seattle, Wash.	2,222	132,423	41,783	29,912	204,118
Vancouver, Wash.	571	(43,726)	(46,644)	(19,289)	(109,659)
King Co., Wash.	1,658	161,314	67,429	(7,640)	221,103
Bellevue, Wash.	146	8,448	4,818	(715)	12,551
Total	5,513	337,309	173,607	55,780	566,696
Total	113,156	8,092,269	8,736,804	5,493,404	22,322,477

^aEach year's surplus or deficit is the difference between the administration fee received and yearly expenses as shown on a PHA's end-of-fiscal-year operating statement.

^bBecause of a change in its accounting period, this PHA's surpluses and deficits are combined in the second year column of this appendix.

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