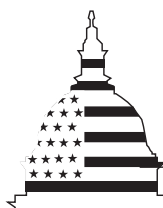


January 2000

MULTIFAMILY HOUSING

HUD's Restructuring Office's Actions to Implement the Mark-to-Market Program



G A O

Accountability * Integrity * Reliability

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Abbreviations

FDIC	Federal Deposit Insurance Corporation
FHA	Federal Housing Administration
GAO	General Accounting Office
HUD	Department of Housing and Urban Development
NCSHA	National Council of State Housing Agencies
OMHAR	Office of Multifamily Housing Assistance Restructuring



B-282631

January 20, 2000

Congressional Committees

The Office of Multifamily Housing Assistance Restructuring (OMHAR) was established within the Department of Housing and Urban Development (HUD) by the Departments of Veterans Affairs and Housing and Urban Development and Independent Agencies Appropriations Act of 1998.¹ The Office was created to administer the “mark-to-market” program, which was also authorized by the act. This program provides the framework to restructure HUD’s portfolio of insured Section 8 multifamily housing projects by “marking” (resetting) rents to market levels and reducing mortgage debt, if necessary, to permit a positive cash flow.² Without restructuring, rents for many of the insured Section 8 multifamily housing projects substantially exceed market levels, resulting in higher subsidies under the Section 8 program. HUD received \$3.8 billion in budget authority for Section 8 project-based subsidies in fiscal year 1998 and an estimated \$4.1 billion in fiscal year 1999.³

¹Referred to in this report as the act (P.L. 105-65, Oct. 27, 1997).

²Insured multifamily housing projects are those with mortgages insured by the Federal Housing Administration (FHA), an agency within HUD. FHA mortgage insurance protects lenders from financial losses stemming from borrowers’ defaults on mortgage loans. In addition to mortgage insurance, many of these properties receive some form of subsidy from HUD. For instance, HUD’s Section 8 program provides rental subsidies for low-income families. These subsidies are linked to either the apartment (project-based) or the resident (tenant-based). The mark-to-market program applies to multifamily housing properties with FHA mortgage insurance and project-based Section 8 assistance.

³Budget authority is the authority provided by law to enter into financial obligations that will result in immediate or future outlays involving federal funds.

The act requires us to audit OMHAR's operations annually during the first 2 fiscal years following the date of enactment. Our initial report, issued in October 1998, described the status of the Office's development, including its preliminary organization and staffing plans, its progress in meeting key operational requirements for implementing the mark-to-market program, and its planned procedures and systems for overseeing the program's implementation.⁴ As agreed with the responsible subcommittees of the Senate and House Appropriations and Banking Committees, this second report focuses on the steps that OMHAR has taken to implement the mark-to-market program. Specifically, it discusses (1) OMHAR's progress in obtaining the staffing resources to implement the program, (2) the status of OMHAR's progress on seven actions that are integral to the program's successful implementation, and (3) whether OMHAR has implemented nine statutory requirements in accordance with the act. We are also reporting on the relationship between OMHAR and other HUD offices, including (1) the extent to which HUD management is involved in directing, reviewing, and approving OMHAR's activities and how this involvement has affected OMHAR's operations; (2) whether OMHAR's Director has complied with the legislative requirements to report to congressional committees if actions by HUD's Secretary interfere with the Office's ability to carry out the mark-to-market program; and (3) whether the other HUD offices from which OMHAR must obtain support have provided the support requested.

The seven actions we reviewed to assess OMHAR's progress in implementing the mark-to-market program were ones we had reviewed for our initial report on OMHAR. These actions included issuing interim and final regulations, developing an operating procedures guide (a manual that sets forth a uniform process to complete work under the program), and selecting organizations (referred to as participating administrative entities) to restructure projects on behalf of OMHAR. The nine statutory requirements that we reviewed to assess whether OMHAR implemented the program in accordance with the act were selected because they were discussed not only in the act but also in congressional debate and the act's accompanying conference report (H.R. 105-297). These requirements included determining market rents and obtaining the tenants' participation in the restructuring process. The actions and the statutory requirements that we reviewed are discussed in the body of the report and in appendixes II and III. We conducted our review from April through December 1999 in

⁴*Multifamily Housing: Progress Made in Establishing HUD's Office of Multifamily Housing Assistance Restructuring* (GAO/RCED-99-5, Oct. 27, 1998).

accordance with generally accepted government auditing standards. (See app. V for a discussion of our scope and methodology.)

Results in Brief

Although OMHAR's organizational and staffing plans have been finalized, they have not yet been fully implemented. As of December 13, 1999, OMHAR had on board 64 of the 75 staff that it had the authority to employ in fiscal year 1999. OMHAR officials attributed the delay in reaching the authorized staffing level in fiscal year 1999 to the normal difficulties associated with staffing an entire office and noted that HUD had taken steps to expedite the hiring process, such as providing OMHAR with priority on all of its personnel actions. OMHAR planned to increase its staffing level to 101 employees in fiscal year 2000. However, language in the Senate Committee report accompanying the fiscal year 2000 HUD appropriations act directed HUD to limit OMHAR to a staffing level of 50 employees until the Office provided the Committee with adequate justification for its staffing needs. Recognizing the implications of the report's language, OMHAR plans to provide additional information on its organization and staffing to the Congress to justify the need for additional staff.

As of December 1999, OMHAR had completed action on five of the seven key aspects of the program's implementation that we reviewed and was taking action on the remaining two. While it has not completed these actions in accordance with the original schedules the Office had developed for completing them, OMHAR officials believe that the slippages did not have much practical effect on the program's implementation because the Office did not begin to receive a large volume of projects to assign for restructuring until the spring of 1999.

The steps that OMHAR has taken thus far on the nine key statutory requirements that we reviewed are generally consistent with the act's requirements. However, given the early stage of the program's implementation, OMHAR's actions for some of these requirements have been limited primarily to establishing program procedures in the mark-to-market regulations and in the operating procedures guide. Consequently, it is too soon for us to determine whether the actual implementation of the procedures will be in accordance with statutory requirements.

Because OMHAR is part of HUD, the actions and the functions of its Director are subject to the review and the approval of the HUD Secretary. For example, various offices within HUD were involved in reviewing and

approving the regulations of the mark-to-market program. However, the issues raised by HUD's offices in reviewing the regulations contributed to a delay of more than 10 months in their issuance. Concerning the legislative requirement that the Director of OMHAR report to the Congress any interference by the HUD Secretary, the Director of OMHAR told us that he has encountered no circumstances in which the HUD Secretary interfered with OMHAR's activities. Furthermore, during the course of our work, we did not become aware of any instances of interference that should have been reported to the Congress. Finally, OMHAR officials believe that HUD's other offices, such as the Office of Housing, have provided the support necessary to meet OMHAR's operational needs.

Background

Over 800,000 units in approximately 8,500 multifamily projects have been financed with mortgages insured by the Federal Housing Administration (FHA) and supported by contracts for project-based Section 8 housing assistance payments. The residents of housing units that receive project-based assistance are required to pay a portion of their income for rent (generally 30 percent), while HUD pays the balance. In 1996, a HUD contractor estimated that, for approximately 63 percent of these multifamily projects, the rents are higher than those of comparable unassisted rental units in the same housing rental market. A main cause of the higher rents is the fact that the government originally paid to develop these properties by establishing rents above market levels and then regularly raised them by applying set formulas that, according to HUD, tended to be generous to encourage the production of new affordable housing. Because HUD makes up the difference between the residents' contributions and the projects' rents, these higher rent levels increase the cost of the Section 8 program to the federal government. HUD estimated that, if no actions were taken, by 2007 the annual cost of renewing project-based Section 8 contracts would rise to approximately \$7 billion, or about one-third of HUD's total budget. On the other hand, if the Section 8 assistance were simply reduced or eliminated, many of the FHA-insured properties could lack sufficient revenues to cover their operating expenses and payments on existing mortgages. As a result, the owners of many properties would likely default on their mortgage payments, resulting in substantial claims to FHA and possibly leaving tenants without adequate affordable housing.⁵

⁵When a default occurs on an insured loan, a lender may "assign" the mortgage to HUD and receive payment from FHA for an insurance claim.

To address the increasing costs to the federal government of insured Section 8 housing, in fiscal years 1996 and 1997, the Congress established mark-to-market demonstration programs to test various methods of restructuring the financing of these properties. In October 1997, the Congress extended the demonstration program through fiscal year 1998 and created the permanent mark-to-market program for projects with above-market rents and project-based Section 8 contracts expiring in October 1998 or later.⁶ The program's goals include preserving the affordability and the availability of low-income rental housing while reducing the long-term costs of Section 8 project-based assistance, resolving the problems affecting financially and physically troubled projects, and correcting management and ownership deficiencies. The October 1997 act also established OMHAR within HUD to administer the program. As required by the act, the Office is under the management of a Director, who was nominated by the President on September 29, 1998, and confirmed by the Senate on October 21, 1998. The act authorizes the mark-to-market program and the Office, including the Director's position, through September 30, 2001. After that time, both the program and the Office will terminate, and any outstanding mark-to-market responsibilities will be transferred to HUD.

The act directs the Office to select capable organizations, referred to as participating administrative entities, to carry out restructuring under the mark-to-market program on behalf of the federal government. This restructuring generally involves resetting rents to market levels and reducing mortgage debt, if necessary, to permit a positive cash flow. Among the participating administrative entities' responsibilities is developing a mortgage restructuring and rental assistance sufficiency plan for each mark-to-market project. Among other things, this plan is to restructure the project-based rents or provide for tenant-based assistance, require the project's owner to provide or contract for competent management of the project, and require the owner to maintain affordability and use restrictions on the project for at least 30 years. Appendix I describes the mark-to-market process in more detail.

HUD published a Request for Qualifications on August 17, 1998, in the *Federal Register* to solicit proposals from organizations interested in

⁶The Multifamily Assisted Housing Reform and Affordability Act of 1997 was enacted in title V of P.L. 105-65. Subtitle A of title V of the 1997 act contains the FHA-Insured Multifamily Housing Mortgage and Housing Assistance Restructuring Program.

becoming participating administrative entities. Organizations that are eligible to become participating administrative entities include public agencies (such as state housing finance agencies or local housing agencies), nonprofit organizations, other entities (including law firms and accounting firms), or a combination of such organizations that meet the act's criteria. However, if a for-profit organization is selected as a participating administrative entity, it is required to enter into a partnership with a public-purpose entity (including HUD). The criteria to select organizations include such requirements as experience in working directly with residents of low-income housing projects and community-based organizations; experience with and capacity for multifamily housing restructuring and financing; a history of stable, financially sound, and responsible administrative performance; financial strength in terms of asset quality, capital adequacy, and liquidity; and a demonstrated ability to carry out mark-to-market responsibilities in a timely, efficient, and cost-effective manner; as well as other criteria established by OMHAR.

OMHAR Has Developed, but Not Fully Implemented, Its Organization and Staffing Plans

OMHAR has developed its organization and staffing plans, which include a headquarters office, four field offices, and a total staffing level of 101 employees, on the basis of the projected workload for the mark-to-market program and other factors. Although the organizational and staffing plans have been finalized, they have not yet been fully implemented; as of December 13, 1999, OMHAR had 64 staff on board. The Office and HUD have taken some steps to overcome specific barriers to hiring staff for OMHAR. To implement its staffing plans, OMHAR was authorized to employ 75 staff in fiscal year 1999 and had requested the full staffing level of 101 employees in HUD's fiscal year 2000 budget proposal to the Congress. However, language in the Senate Committee report that accompanied the fiscal year 2000 HUD appropriations legislation directed HUD to limit OMHAR to a staffing level of 50 employees until the proposed staffing level was adequately justified. Recognizing the implications of the report's language, OMHAR plans to provide additional information on its organization and staffing to the Congress to justify the need for additional staff.

OMHAR Has Developed Its Organization and Staffing Plans Based on Various Analyses, but Not All Planned Staff Have Been Hired

OMHAR has planned an organizational structure that calls for a full staffing level of 101 employees. Of these, the Office had the authority to employ 75 staff in fiscal year 1999 and had requested the full level of employees in HUD's fiscal year 2000 budget proposal to the Congress. OMHAR developed its organization and staffing plans for headquarters through discussions within the Office and with various program and personnel experts to identify the positions needed to carry out its program and administrative responsibilities.

Under the planned structure, slightly less than half of OMHAR's total number of 101 employees will be located at its headquarters office in Washington, D.C. The remaining staff will be distributed among three OMHAR field offices in Chicago, New York, and San Francisco, and a fourth field office, responsible for the southeast region of the United States, which is co-located with the Washington headquarters office.⁷ OMHAR based its organization and staffing plans for the field offices on analyses of several factors. Specifically, OMHAR determined where the field offices would be located by considering such analyses as the timing and the volume of the estimated mark-to-market program workload in each state, the presence or absence of a HUD hub office in the same city,⁸ the accessibility by air, and the ease of ground transportation in the area. Once the locations were determined, OMHAR estimated the staffing needs for each field office according to analyses of field office responsibilities, the number of mark-to-market projects expected for each area, and the number of hours required to complete each project. OMHAR finalized its plans for locating the four field offices in January 1999. According to OMHAR officials, the New York, Chicago, and Washington, D.C., offices were operational in June 1999, and the San Francisco office became operational in August 1999. Although none of the field offices had been fully staffed by the end of fiscal year 1999, all of the 29 field office positions authorized for that year had been staffed by December 13, 1999.

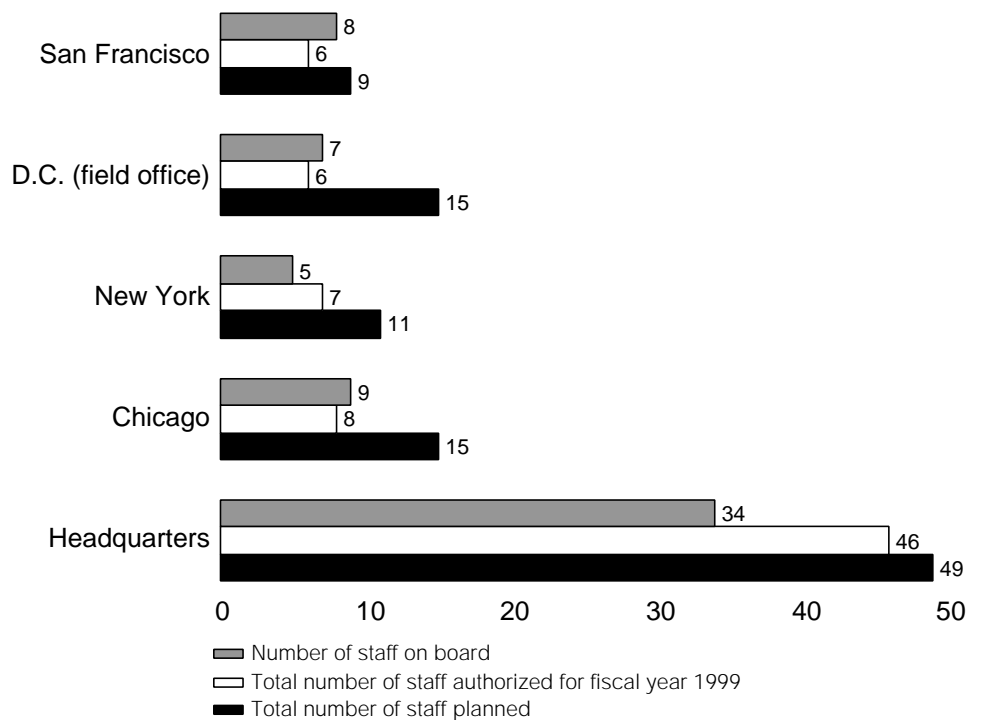
As of December 13, 1999, OMHAR had 64 staff on board, an increase of 18 employees over the number on board at the end of September 1999. According to OMHAR officials, about 20 percent of the staff on board were

⁷Under the fiscal year 1999 staffing plan, 46 positions (61 percent of the authorized level of 75) were located at OMHAR's headquarters office, and the remaining 29 positions (39 percent of the 75) were located in the field offices.

⁸"Hub" refers to a HUD field office with multifamily housing program responsibilities.

previously employed by HUD, and the remaining staff were hired from outside of HUD. Figure 1 shows the number of staff planned for each location and the number hired as of December 13, 1999.

Figure 1: Number of OMHAR Staff Planned and Number of Staff On Board, December 13, 1999



Note: Two of the staff positions counted among the field office positions are not allocated to any specific field office and therefore are not reflected in this figure. These positions are the field manager and the mark-to-market ombudsman. According to OMHAR officials, the planned distribution of staff among the field offices is subject to change as workload projections are revised.

Source: GAO's analysis of OMHAR's data.

Of the positions remaining to be filled as of December 1999, 15 were in headquarters and 22 were in the field offices. Most of the open positions in the field offices were for debt-restructuring specialists, who work with participating administrative entities as they carry out project restructurings. According to OMHAR officials, the Office's hiring process focused first on positions that were necessary to build an infrastructure for the Office and the mark-to-market program and then on positions that would be needed as the program began to be implemented. Considering

that project restructurings were just beginning to get under way and none were completed by the end of fiscal year 1999, OMHAR officials thought they had had adequate staff to carry out the Office's functions up to that point. They expected to have the remaining 11 positions that were authorized for fiscal year 1999 but not staffed as of December 13, 1999, either advertised or filled by the end of December 1999.

Congressional Action Could Limit OMHAR's Staffing Level

OMHAR has requested a full staffing level of 101 employees in HUD's fiscal year 2000 budget proposal to the Congress. However, language in the Senate report (S. 106-161) that accompanied the fiscal year 2000 HUD appropriations legislation directed HUD to limit OMHAR to a staffing level of 50 employees until the Office provides "adequate justification for its staffing" needs to the Senate Committee on Appropriations. In its report, the Committee stated that OMHAR's salaries and expenses had not been adequately justified and that the justification did not reflect its roles and responsibilities as envisioned by the mark-to-market legislation. Although no staffing limit for OMHAR was specified in the fiscal year 2000 HUD appropriations act itself, language in the conference report (H.R. 106-379) that accompanied the act indicates that OMHAR must comply with the Senate report's language because it was not addressed to the contrary in the conference report. In response to this limitation, OMHAR officials planned to provide more detailed information on the Office's organization and staffing to the Congress by the end of December 1999. OMHAR officials stated that they expected this additional information to justify the need for additional staff.

OMHAR Has Taken Steps to Overcome Perceived Barriers to Its Ability to Hire Staff

OMHAR officials said that the Office has been successful in attracting exceptionally qualified individuals from within HUD, other agencies, and private industry. Although several positions remain open, these officials maintain that staffing an entire office takes time, particularly when the process has to be done in accordance with many regulations and requirements. However, they also thought that some specific barriers have hindered the Office's ability to hire qualified staff.

First, OMHAR officials stated that the act's language regarding post-employment provisions for OMHAR employees could be interpreted too stringently.⁹ They said that the provisions' wording could be interpreted by potential applicants to mean that an OMHAR employee could not take a job with a financial institution or local government for 2 years after leaving OMHAR. The officials said that such a strict interpretation by potentially interested parties might hinder OMHAR's ability to attract highly qualified staff for its senior positions but that it is difficult to determine the extent to which this factor had actually hindered their hiring ability. According to them, for fiscal year 1999, only five of OMHAR's positions, by virtue of their pay levels, were subject to these provisions, and all but one of these had been filled as of December 13, 1999. Another barrier that OMHAR officials said had impeded the Office's ability to hire staff was its lack of Schedule A hiring authority. Such authority enables agencies to hire staff without administering an examination. However, on January 29, 1999, HUD received authority to hire employees on OMHAR's behalf under the Department's own Schedule A hiring authority. According to HUD, subsequent to this agreement, the OMHAR Director decided to primarily use competitive hiring procedures for personnel actions so the process could withstand public scrutiny and avoid any charge of politicization. Finally, at the time some OMHAR positions were advertised, HUD had not yet made a decision on reemployment rights for OMHAR employees, which would give them the right to employment within the Department upon completion of their work at OMHAR. According to OMHAR officials, this fact limited the interest of experienced HUD staff in working for OMHAR. However, in February 1999, the HUD Deputy Secretary approved reemployment rights for OMHAR career employees, thus removing this issue as a potential barrier.

OMHAR and HUD have also taken other actions to expedite the hiring process. For example, OMHAR officials told us in May 1999 that HUD's Office of Human Resources had made a commitment to provide OMHAR with priority on all of its personnel actions and to assign two employees to work on those actions. OMHAR officials stated that this commitment has

⁹Section 576 of the act states that, for 2 years after leaving the Office, any OMHAR employee who was paid more than the lowest rate for a position above the GS-15 level cannot accept compensation from any party (other than a federal agency) having any financial interest in any mortgage restructuring and rental assistance sufficiency plan or comparable matter in which the employee had direct participation or supervision. In effect, according to OMHAR officials, this provision applies to any OMHAR employee whose base salary exceeds that of the highest GS-15 level.

decreased the time needed to fill an OMHAR position. According to HUD's Office of Administration, the number of workdays to fill an OMHAR position has averaged 39 workdays, compared with an average of 50 workdays for other HUD positions. In addition, for fiscal year 1999, HUD gave OMHAR blanket authority to fill all 75 of the positions authorized for that year, rather than seeking authority for each position individually, as is normally required.

**OMHAR Has
Accomplished Several
Key Actions, but Many
Were Completed
Behind Schedule**

Since our October 1998 report on the establishment of OMHAR, the Office has taken steps to complete each of the seven actions we reviewed and had completed five of them as of December 1999. For example, both the program's operating procedures guide and the selection process for OMHAR's administrative partners—the participating administrative entities—have been completed. Furthermore, by the end of May 1999, OMHAR began assigning multifamily housing projects to the participating administrative entities for restructuring. As of December 13, 1999, OMHAR had assigned to the participating administrative entities 52 percent of the 997 projects that had entered the program, but, as of that date, none of the restructurings had been completed.

Although OMHAR has completed five of the seven actions we reviewed, all of them were completed behind the Office's original schedule. Furthermore, the two remaining actions are taking longer to complete than OMHAR originally anticipated. For example, the act required OMHAR to publish the program's final regulations no later than 3 months after the appointment of a Director, which occurred in October 1998.¹⁰ While OMHAR planned to issue these regulations by January 1999, they had not been published as of December 13, 1999.¹¹ Furthermore, OMHAR completed the process to select the participating administrative entities behind schedule. OMHAR expected to complete this process by October 29, 1998, but the selected public entities (i.e., state and local housing finance agencies) were not announced until January 21, 1999. Nonpublic entities were selected in May 1999. Before the participating administrative entities could receive Section 8 projects to restructure, they had to sign contracts, called portfolio-restructuring agreements, with OMHAR. The Office had planned to enter into these contracts with the entities as soon as possible after the selection process was complete. However, OMHAR's contract negotiations with potential public participating administrative entities proved to be a lengthy process, taking several months to sign contracts with the selected state and local housing finance agencies.¹² Because projects could not begin to be restructured until this process was complete, OMHAR's delay in selecting the entities and entering into contracts with them delayed the program's implementation.

According to OMHAR officials, the delay in accomplishing mark-to-market actions was due, in part, to the normal challenges associated with starting a new organization. They also cited specific reasons certain actions were delayed. For example, they said the delay in selecting the participating administrative entities was due to the Office's compliance with the legislative requirement to give preference to public agencies. While

¹⁰Prior to issuing final regulations, the mark-to-market program operated under interim regulations, which were published September 11, 1998, and became effective October 13, 1998.

¹¹OMHAR had originally planned to issue the final regulations in October 1998 but revised the schedule because the OMHAR Director was not appointed until October 21, 1998.

¹²OMHAR began negotiating contracts with individual public participating administrative entities in March 1999. As of December 13, 1999, OMHAR had reached agreement with 37 public agencies and was still negotiating with 9 public agencies. Also, as of that date, six public agencies had elected not to participate in the program because they could not reach agreement with OMHAR on such contract issues as compensation or state-specific legal concerns.

OMHAR officials told us that many of these agencies were notified in October 1998 that they were qualified to participate in the program (conditioned on their acceptance of OMHAR's fee structure), the official announcement of the 52 selected public agencies was not made until January 1999, after those agencies that had been initially rejected could resubmit their proposals to become qualified. According to HUD, OMHAR worked closely with rejected agencies to try to qualify them. OMHAR officials also acknowledged that signing portfolio-restructuring agreements with the participating administrative entities took much longer than originally expected. They said the process of working cooperatively with the public agencies to develop standardized contract provisions was time-consuming. OMHAR officials also cited two reasons for the delay in issuing the final regulations—the issues raised by various HUD offices and the Office of Management and Budget during a lengthy review and clearance process and the fact that the regulations included Section 8 contract renewal provisions, which were not under the Office's direct control. While OMHAR officials agreed that certain mark-to-market actions were completed behind the Office's original schedule, they did not believe that the slippages had much practical effect on the program's implementation. They believed that the Office was being prudent in implementing the program by first establishing an infrastructure before assigning projects for restructuring. Furthermore, the Director of OMHAR stated that the Office did not begin to receive a large volume of projects to assign for restructuring until the spring of 1999.

Nevertheless, because of delays in implementing the program, OMHAR will have to extend some expiring Section 8 contracts at the projects' current rent levels beyond the time frame allowed in the mark-to-market regulations. The regulations allow OMHAR to extend a contract for 1 year at a project's current rents to provide the participating administrative entity time to restructure it. However, OMHAR is currently preparing a waiver that would allow it to continue the higher rents. In October 1999, OMHAR officials estimated that the additional Section 8 costs for 34 projects expected to receive contract extensions for longer than 1 year would be about \$4.1 million. It should be noted, however, that these increased costs will be offset, at least somewhat, to the extent that payments to cover HUD's costs for restructuring projects, such as claims to FHA and fees to the participating administrative entities, are also delayed.

In its comments on our draft report, HUD reiterated that, while our report implies that its delay in signing contracts with the participating administrative entities caused a delay in the program's implementation, in

HUD's view, the real question was whether the process of contracting with those entities was carried out in the right manner. HUD stated that OMHAR had negotiated standardized contract provisions with participating administrative entities and their trade groups and had honored congressional priorities.

OMHAR's Planned Procedures Have Been Generally Consistent With Statutory Requirements

We found OMHAR's actions for implementing the nine statutory mark-to-market requirements that we reviewed, such as determining market rents and obtaining tenant participation, have been generally consistent with the act's requirements. However, given the early stage of the program's implementation, OMHAR's actions for some of these requirements have largely been limited to establishing program procedures in the mark-to-market regulations and in the operating procedures guide. The National Council of State Housing Agencies (NCSHA) and some state and local housing finance agencies we contacted have questioned whether OMHAR implemented one of the nine statutory requirements we reviewed, the process for selecting participating administrative entities and allocating projects to them, in accordance with the statute.¹³ (For information on OMHAR's actions relating to the other eight mark-to-market statutory requirements that we examined, see app. III.)

The act requires OMHAR to select participating administrative entities according to certain criteria, such as demonstrated experience with multifamily financing, the financial strength to carry out the mark-to-market restructurings, and cost-effectiveness, as well as other criteria established by OMHAR.¹⁴ In conjunction with this requirement, the act specifically requires that OMHAR provide a reasonable period during which it will consider proposals only from state or local housing finance agencies and that OMHAR select such an agency without considering other applicants if it determines that the agency is qualified. The act states that this period must be of sufficient duration for OMHAR to determine whether any state or local housing finance agencies are interested and qualified. Furthermore, the act states that if a state or local housing finance agency is

¹³NCSHA is a national organization representing 43 state and local housing finance agencies.

¹⁴In addition to stating that the Secretary of HUD has these responsibilities, the act requires the Secretary to carry out the mark-to-market responsibilities through the OMHAR Director. Accordingly, we refer to OMHAR rather than the Secretary here, because OMHAR is actually responsible for carrying out these functions.

selected as the participating administrative entity, that agency will be responsible for restructuring such projects in that jurisdiction as may be agreed upon by that agency and OMHAR.

The Request for Qualifications required entities, both public and nonpublic, that were interested in participating in the mark-to-market program to submit applications to OMHAR by September 16, 1998. According to OMHAR, the applications were reviewed in two phases, with exclusive priority given to public agencies during the initial phase. After reviewing the applications from public agencies, the Secretary of HUD announced on January 21, 1999, that 52 state and local agencies had been selected to implement the mark-to-market program. However, in making this announcement, the Director of OMHAR told us that the Office only determined that these public agencies were “technically qualified” to participate in the program, not actually chosen to perform restructuring activities. Prior to actually participating in the program, these agencies must sign a contract, referred to as a portfolio-restructuring agreement, with the Office. This agreement sets forth the terms the entities must follow in carrying out the restructuring actions and also the compensation OMHAR would pay them. According to the standard portfolio-restructuring agreement for public participating administrative entities, OMHAR will compensate them with a uniform base fee, reimburse certain expenses, and provide incentive fees if they achieve established goals. According to OMHAR officials, the compensation amounts were based on analyses of information, including a survey of 20 firms’ estimated costs to complete a restructuring transaction.

As of December 13, 1999, OMHAR had signed portfolio-restructuring agreements with 37 public agencies. As of that date, OMHAR had not been able to reach agreement with the other selected state and local agencies because of such factors as disagreements concerning the compensation they would receive to perform the restructurings, concerns about the operating procedures guide, and state-specific legal issues. While OMHAR’s Director told us that the Office was still trying to reach agreements with the other public agencies, six public agencies had elected not to participate in the program because of their inability to reach agreements with OMHAR. Approximately 30 percent of the projects that had entered the program as of December 13, 1999, were located in jurisdictions where the public agencies had been unable to reach agreement with OMHAR by that date or where the agencies subsequently elected not to participate in the program.

We contacted selected state and local housing finance agencies to obtain their views on negotiating contract terms with OMHAR.¹⁵ Of the 10 state or local agencies we spoke with, 8 did not believe that OMHAR's proposed compensation was fair. In addition to concerns with compensation, the three agencies that we contacted that had decided not to participate in the program cited the prescriptive nature of OMHAR's operating procedures guide as a reason not to participate. We also obtained information from six other public agencies that, as of October 1999, had not reached agreement with OMHAR. While one agency could not reach agreement with OMHAR because of compensation issues, the other five agencies cited various legal issues as reasons for not signing the portfolio-restructuring agreement.¹⁶

For the 16 nonpublic entities that applied to participate in the mark-to-market program, OMHAR began reviewing their proposals on January 22, 1999, the day after the announcement that the 52 public entities had been selected. On May 4, 1999, OMHAR sent 11 of the nonpublic entities a letter saying they were qualified to participate in the program and a bid package soliciting additional information. OMHAR received proposals from 8 of the 11 qualified entities, and subsequently it requested, on two occasions, that they provide their best and final offers. After reviewing the proposals, OMHAR selected three of these entities to serve as participating administrative entities. OMHAR and these three entities signed contracts that became effective on June 30, 1999. As of December 13, 1999, OMHAR was in the process of conducting a second nonpublic bid and expected to sign contracts with the successful bidders by the end of December 1999. HUD stated that while some states believe that OMHAR's fee structure is not reasonable, the fact that nonpublic participating administrative entities have accepted lower fees than those OMHAR has offered to public entities demonstrates that OMHAR's fee determinations have been accurate.

¹⁵We contacted 10 of the 52 state and local housing finance agencies that qualified to participate in the program. Four had signed portfolio-restructuring agreements with OMHAR, three had not yet reached agreement, and three had elected not to participate in the program. We note that the information obtained from these agencies does not necessarily reflect the views of all the public agencies or all the nonpublic entities selected to participate in the program.

¹⁶For example, one state agency cited language in the portfolio-restructuring agreement that required the agency to indemnify OMHAR for willful misconduct, negligence, or actions not permitted by the terms of the agreement. According to that agency, this requirement was prohibited by its state constitution. Another state agency maintained that the portfolio-restructuring agreement limited its ability to choose counsel for representation on mark-to-market issues.

As of December 13, 1999, OMHAR had assigned 374 projects to 28 public agencies for restructuring, and an additional 145 projects were pending acceptance by the participating administrative entity to which they had been assigned. Additionally, OMHAR had assigned 83 projects to nonpublic entities in eight states where no public agency had elected to participate in the program and 13 projects in two states where the public agency initially elected to participate but later decided not to. In one state, OMHAR assigned 29 projects to a nonpublic entity while it was still negotiating with the state agency, but the agency had not yet signed a portfolio-restructuring agreement.¹⁷

NCSHA representatives and some state and local housing finance agencies that we contacted have questioned whether OMHAR's selection of participating administrative entities has been conducted in accordance with statutory requirements. In particular, the Council's Executive Director has expressed the view that by establishing a uniform compensation fee structure to which all public entities must agree, OMHAR has not complied with the act's requirement to reimburse participating administrative entities for all reasonable expenses they incur. While he maintained that HUD is required to challenge specific state costs if it believes they cannot be substantiated, HUD cannot reject a state's costs just because they are higher than another state's costs or an estimate from a private sector bidder. The NCSHA representative also said the Congress did not condition the state and local agency priority on those agencies accepting costs equal to or lower than private sector costs. He said the Congress did not intend the mark-to-market program to go to the lowest bidder. Representatives from NCSHA also believed that OMHAR violated the act when it assigned properties to a nonpublic entity for restructuring in a jurisdiction where it was still negotiating contract terms with the state agency. In their view, the act requires OMHAR to assign qualified and willing state agencies the projects within their jurisdictions to restructure and the act does not allow OMHAR to assign projects to nonpublic entities without the consent of the state.

While we recognize that OMHAR's actions in selecting participating administrative entities have generated considerable concern, nonetheless,

¹⁷Also, OMHAR assigned 10 projects in two states to nonpublic entities, pending formal approval of the public agencies in those locations, and assigned 13 projects to a nonpublic entity in two other states because of issues concerning capacity and conflict of interest with the public agencies in those locations.

we believe that OMHAR's actions have been consistent with the statutory requirement that it give priority to state and local agencies. Not only did OMHAR establish a period during which it only considered applications from state and local housing finance agencies, it has also continued to try to reach agreements with these agencies before assigning any projects in their jurisdictions to nonpublic entities for restructuring. While the process that OMHAR followed has proven to be lengthy and has led to disagreements between OMHAR and state and local housing agencies, in our view, it is permissible under the law.

We agree with the NCSHA representatives that the act does not require the mark-to-market program to go to the lowest bidder, but we do not agree that the act precludes OMHAR from establishing a uniform fee structure. The act requires that a prospective participating administrative entity be evaluated for, among other things, "cost-effectiveness" and that a participating administrative entity be compensated for its "reasonable expenses." However, the act neither mandates the method OMHAR is to use to determine "cost-effectiveness" nor mandates the method to determine the types or the amount of expenses that are considered "reasonable." OMHAR has the discretion to determine what constitutes "cost-effectiveness" as well as "reasonable costs" as part of its overall statutory duty "to determine whether any state housing finance agencies or local housing agencies are interested and qualified" to participate in the mark-to-market program.

With regard to NCSHA's concern that OMHAR had assigned projects to a nonpublic entity while still negotiating contract terms with a public agency, OMHAR officials said the Office did this because there was an urgent need to restructure properties in the state and OMHAR could not reach agreement with the state housing finance agency on compensation issues. In our view, because OMHAR had yet to reach an agreement with the state agency in this case, OMHAR was under no obligation to (and, indeed, could not) assign any projects to it. Even if that agency were to become a participating administrative entity in the future, the number of projects assigned to it would be that number "as may be agreed upon by the participating administrative entity and [OMHAR]." Should OMHAR find that an agreement could not be reached, it then would have the option of assigning projects to a nonpublic participating administrative entity. The act does not require that OMHAR receive permission from the relevant state or local housing finance agency before assigning projects to a nonpublic entity.

HUD Offices Were Involved in OMHAR's Key Tasks and Provided Support for Its Operations

While other HUD offices were involved in three of OMHAR's key tasks that we reviewed, their involvement consisted primarily of reviewing OMHAR's proposals and providing comments on them. According to HUD officials, these reviews were aimed at ensuring that OMHAR's actions met the act's requirements and were consistent with HUD's policies. However, these reviews contributed to OMHAR's delay in issuing its regulations for the mark-to-market program. With regard to the obligation of the Director of OMHAR to report to the Congress any interference by the HUD Secretary in OMHAR's activities, the Director indicated that there had been none. Likewise, we did not encounter any instances of interference during our review. With respect to support from other HUD offices, officials from both HUD and OMHAR stated that these offices had provided sufficient and timely support when OMHAR requested it.

HUD's Involvement in OMHAR's Key Tasks Was Primarily in the Form of Reviews and Clearances

Section 573(b) of the act specifies that the OMHAR Director's determinations, actions, issuance of regulations, and functions are subject to the HUD Secretary's review and approval. We reviewed HUD's involvement in three of OMHAR's key tasks: developing the program's regulations, the Request for Qualifications for participating administrative entities, and the program's operating procedures guide. For these three tasks, the involvement of other HUD offices consisted primarily of reviewing OMHAR's proposals and commenting on them.

Numerous HUD offices were involved in OMHAR's development of the program's regulations, with primary involvement coming from the offices of Housing and General Counsel. For example, these offices drafted the interim regulations, issued in September 1998, because OMHAR was not yet operational. The Office of Housing submitted the interim regulations to other HUD offices for review and clearance. The Office of General Counsel then directed the interim regulations through an abbreviated review and clearance process.

HUD offices also provided review and clearance of the final mark-to-market regulations, which were combined with final regulations on project-based Section 8 contract renewals.¹⁸ However, concerns raised during their

¹⁸OMHAR later decided to separate the mark-to-market regulations from the Section 8 contract renewal regulations. The Director of OMHAR stated that this was done because the Office of Housing reconsidered portions of the Section 8 regulations when the mark-to-market regulations were nearing final approval.

review of the regulations added to the delay in issuing them. Under the act, the regulations were required to be issued no later than January 21, 1999. OMHAR distributed the final regulations to HUD offices on March 9, 1999. As of December 13, 1999, final regulations had not been issued, but OMHAR officials expected them to be published by the end of the year.

According to an official in HUD's Office of General Counsel, the complexity of the concerns raised by other HUD offices and the need to obtain public comments on the regulations were the main reasons for the delay. In particular, five HUD offices raised concerns with the final regulations that needed to be resolved before they could be approved. For example, HUD's Office of Public and Indian Housing would not approve the regulations until OMHAR clarified which residents would be eligible for tenant-based assistance in projects with expiring Section 8 contracts. Furthermore, the Office of Chief Financial Officer would not approve the regulations until a risk assessment of the mark-to-market program had been completed.

According to HUD and OMHAR officials, HUD offices were also involved in reviewing and approving draft versions of the Request for Qualifications for soliciting participating administrative entities. For example, HUD's Office of General Counsel reviewed the Request for Qualifications to verify that it conformed to the statutory language that state and local public agencies were given priority consideration over nonpublic entities. HUD's Office of Inspector General disagreed with the draft Request for Qualifications because it did not solicit sufficient historical information on the financial and administrative capacity of the organizations applying for selection to become participating administrative entities. In response to the Inspector General's concern, OMHAR changed the Request for Qualifications. HUD and OMHAR officials stated that no other HUD offices or officials were involved in actually selecting participating administrative entities, except for a request made by the Secretary's Office that OMHAR demonstrate proper management and oversight for both public and nonpublic entities.

Developing OMHAR's operating procedures guide involved several HUD offices, with primary input coming from the offices of Housing and General Counsel. For example, OMHAR held a departmental retreat with these offices to resolve key implementation issues in the guide. OMHAR also distributed the guide to these offices and the Office of Inspector General for review and comment. However, to expedite issuing the guide since informal reviews by relevant HUD offices had already been obtained, OMHAR obtained approval from HUD's Deputy Secretary to forgo the normal review and clearance process.

**OMHAR Director Reports
No Interference by the HUD
Secretary**

Section 573(d)(2) of the act states that the Director of OMHAR is to report to the Congress any actions by the HUD Secretary that interfere with the Office's activities. Specifically, the act requires the reporting of any action that interferes with the Director's ability to perform his duties or that affects the administration of the mark-to-market program, including proposed actions by the Director that are overruled by the Secretary. The Director stated that he is mindful of his responsibilities under the statutory requirements and would report any actions that would interfere with his ability to perform any duties in administering the mark-to-market program. However, according to the Director of OMHAR, HUD's Secretary had not interfered in any activities as of December 13, 1999. Moreover, in the course of our work, we did not identify any incidences of HUD's interference that should have been reported to the Congress.

**HUD Provided the
Necessary Support for
OMHAR to Meet Its Needs**

Officials from both OMHAR and other HUD offices said that HUD has provided sufficient support for OMHAR to meet its operational needs. For example, the Office of Housing provided staff, space, equipment, and technical expertise in the initial months of OMHAR's operations. In addition, HUD's Office of Procurement and Contracting has supported OMHAR by fulfilling its contracting needs, including hiring, at its request, an employee to work primarily on its contracting activities. While HUD's Office of Procurement and Contracting can assign this person other work, OMHAR's needs are expected to take priority. Furthermore, HUD's multifamily hubs have screened owners for initial eligibility before allowing them to participate in the mark-to-market program.

Agency Comments

We provided HUD with a draft of this report for its review and comment. HUD's written comments are in appendix IV. HUD generally agreed that the draft report accurately describes OMHAR's efforts to date to implement the mark-to-market program. However, HUD expressed the concern that the scope of our evaluation precluded a fully balanced picture from being achieved and requested that any additional review of its implementation of this program be expanded to more accurately portray the complex issues and conflicting goals that OMHAR has had to balance. In this regard, HUD cited a number of actions that OMHAR has taken since October 1998 to implement the mark-to-market program and noted that it is confident that the extra time spent in setting up the proper infrastructure and protocols will allow OMHAR to more efficiently respond to issues that arise during the program's implementation. We do not agree that the scope of our

evaluation precluded us from presenting a balanced view of OMHAR's implementation of the program. While we did not discuss every action that OMHAR has taken since October 1998, when we previously reported on the program's status, we believe our report does discuss most, if not all, of the key actions that OMHAR has taken to implement the mark-to-market program, including the vast majority of those cited by HUD.

HUD also stated that OMHAR was thorough in its analysis of the compensation participating administrative entities should receive. As discussed in our report, while some states believed that OMHAR's fee structure was not reasonable, HUD maintained that the fees accepted by the nonpublic participating administrative entities demonstrate the accuracy of OMHAR's fee determinations. Lastly, HUD stated that, while our report implies that its delay in signing contracts with the participating administrative entities delayed the program's implementation, the real question was whether the process of contracting with those entities was carried out in the right manner. HUD pointed out that OMHAR had negotiated standardized contract provisions with participating administrative entities and their trade groups and had honored congressional priorities. We have incorporated these comments, as well as technical changes that HUD provided, into our report, as appropriate.

We are sending copies of this report to the Honorable Andrew M. Cuomo, Secretary of Housing and Urban Development, and to the Honorable Ira G. Peppercorn, Director of the Office of Multifamily Housing Assistance Restructuring. We will make copies available to others on request. If you or your staff have any questions about this report, please call me at (202) 512-7631. Major contributors to this report are listed in appendix VI.



Stanley J. Czerwinski
Associate Director, Housing and
Community Development Issues

List of Committees

The Honorable Wayne Allard
Chairman
The Honorable John F. Kerry
Ranking Minority Member
Subcommittee on Housing and Transportation
Committee on Banking, Housing,
and Urban Affairs
United States Senate

The Honorable Christopher S. Bond
Chairman
The Honorable Barbara A. Mikulski
Ranking Minority Member
Subcommittee on VA, HUD, and
Independent Agencies
Committee on Appropriations
United States Senate

The Honorable Rick A. Lazio
Chairman
The Honorable Barney Frank
Ranking Minority Member
Subcommittee on Housing and
Community Opportunity
Committee on Banking and
Financial Services
House of Representatives

The Honorable James T. Walsh
Chairman
The Honorable Alan B. Mollohan
Ranking Minority Member
Subcommittee on VA, HUD,
and Independent Agencies
Committee on Appropriations
House of Representatives

Overview of the Mark-to-Market Process

In general, the process to be followed under the mark-to-market program, as outlined in the Office of Multifamily Housing Assistance Restructuring's (OMHAR) operating procedures guide, has 13 phases: (1) project assignment to participating administrative entity, (2) kick-off meeting, (3) notice of first restructure plan consultation meeting, (4) tenants' comments, (5) consultation meeting, (6) physical condition assessment, (7) second tenants' meeting, (8) underwriting process, (9) submission of the draft restructuring plan, (10) restructuring plan execution, (11) notice of completion of restructuring plan, (12) closing, and (13) post-closing document distribution.¹

1. *Project Assignment to Participating Administrative Entity:* The mark-to-market process is initiated when an owner of Section 8 housing notifies the HUD multifamily hub or program center of the intent to participate in the mark-to-market program.² The hub or program center screens the owner and the project to determine initial eligibility and then forwards eligible projects to OMHAR headquarters for assignment to a participating administrative entity. The participating administrative entity is responsible for making a complete and ongoing assessment of the eligibility of the owner and the project.

2. *Kick-off Meeting:* After headquarters assigns the project, the participating administrative entity contacts the owner and provides the ground rules, the forms, and other information. At this time, the participating administrative entity also sets the date for the kick-off meeting, which must be held within 15 days following the owner's receipt of that information. At the meeting, the participating administrative entity explains the restructuring process and distributes copies of all closing documents, among other things.

3. *Notice of First Restructure Plan Consultation Meeting:* Immediately following the kick-off meeting, the participating administrative entity (or the owner on the administrative entity's behalf) must send a Notice of First Restructure Plan Consultation Meeting to the tenants and other interested parties. The notice states that the owner has elected to participate in the mark-to-market program; when the project-based Section 8 contract is

¹This 13-phase process applies only to "full" restructurings, under which both a project's rents and its mortgage are restructured.

²HUD's field office structure for delivering multifamily housing services consists of 18 jurisdictional hubs with staff stationed in 33 program centers.

scheduled to expire; how the recipients can give comments to the participating administrative entity regarding the property's physical condition and other matters; and the date, the time, and the place of a public meeting to be held no sooner than 20 days, but within 40 days, following the date of the notice.

4. *Tenants' Comments:* After receiving the notice, the tenants and other interested parties can provide written comments to the participating administrative entity on such matters as the property's physical condition, the project's management, and whether rental assistance should be project-based or tenant-based.

5. *Consultation Meeting:* Between 20 and 40 days after the notice, the participating administrative entity must conduct a meeting to hear oral presentations and comments by the tenants and other affected parties on the desired contents of a Restructuring Plan, on the owner's evaluation of the project's physical condition, and on any proposed transfer of the project to another owner.

6. *Physical Condition Assessment:* If the owner has not already submitted an evaluation of the project's physical condition, it should be completed soon after the consultation meeting. The participating administrative entity will work with a third-party inspector, who will consider the owner's evaluation as well as comments from the tenants and the local community. The participating administrative entity's inspector must coordinate his or her analysis with the participating administrative entity's third-party appraiser.

7. *Second Tenant Meeting:* The participating administrative entity must develop, in cooperation with the owner, a mortgage restructuring and rental assistance sufficiency plan for each project. Among other information, the plan provides conclusions on the project's new mortgage amount(s), rehabilitation needs, and financial return to the owner. Ten days before submitting the draft restructuring plan to OMHAR for review, the participating administrative entity must hold a follow-up meeting with the tenants and other affected parties so they can comment on the development of the plan. The proposed plan should be available for these parties to inspect at least 20 days before it is submitted to OMHAR for review.

8. *Underwriting Process:* Generally, underwriting is completed within 105 days after the project is assigned to the participating administrative entity.

The participating administrative entity considers the project's finances and completes a Rental Assistance Assessment Plan to determine whether the Section 8 assistance should be renewed as project-based assistance or converted to tenant-based assistance. The participating administrative entity, the owner, and the lender discuss mortgage options. The outcome of this phase is the draft restructuring plan mentioned in the preceding phase.

9. *Submission of the Draft Restructuring Plan:* The participating administrative entity submits the draft restructuring plan to OMHAR for review. OMHAR determines whether to approve, reject, or return the plan for modifications.

10. *Restructuring Plan Execution:* After OMHAR approves the plan, the participating administrative entity sends the owner notification and a restructuring plan commitment. The owner has 30 days after this restructuring commitment is issued to execute it.

11. *Notice of Completion of Restructuring Plan:* Within 10 days after the restructuring commitment is executed, the participating administrative entity must send the project's tenants and other interested parties a notice describing the final restructuring plan and restructuring commitment.

12. *Closing:* The owner, the lender, the participating administrative entity, and HUD sign and record all documents. Closing should be completed within 60 days of executing the restructuring commitment.

13. *Post-Closing Document Distribution:* The closing dockets and the other supporting documents are distributed to HUD officials, loan servicers, asset managers, and others.

Summary and Status of Seven Key Actions Needed to Implement the Mark-to-Market Program

Action	Purpose	Current status
Issue the interim and the final regulations.	To implement the mark-to-market program. The law required the final regulations to be issued before the later of October 27, 1998, or 3 months after the Director of OMHAR had been appointed (§522(a)(2)).	<p>Not completed; behind schedule. The interim regulations were published September 11, 1998, and became effective October 13, 1998. HUD had originally expected to issue the interim regulations by August 1998 and the final regulations in October 1998. However, because OMHAR's Director was not appointed until October 21, 1998, the target date for issuing final regulations was moved back to January 21, 1999, (3 months after the appointment of the Director).</p> <p>As of December 13, 1999, final regulations had not been published, in part, because of issues raised by other HUD offices during their review and clearance of the regulations. According to OMHAR officials, the original time allowed by the act for issuing final regulations was optimistic and did not reflect normal clearance time frames, given the innovative nature and the complexity of the mark-to-market program. OMHAR officials also said that the delay in issuing the regulations had not delayed the program's implementation since the program has been operating under the full authority of the interim regulations. These officials expect the regulations to be published by the end of December 1999.</p>
Solicit and select third parties, referred to as participating administrative entities.	To allow HUD to work with the participating administrative entities, which will actually restructure the mortgages and rental assistance payments of eligible multifamily projects (§513(a)(1)).	<p>Completed behind schedule. HUD published the Request for Qualifications to solicit participating administrative entities on August 17, 1998. In September 1998, OMHAR expected to complete the selection process by October 29, 1998. According to OMHAR officials, many of the public entities were notified in October 1998 that they were qualified to participate in the program. However, HUD did not officially announce the selected public participating administrative entities until January 21, 1999.</p> <p>Proposals from the nonpublic entities were opened after the public entities had been selected. On May 4, 1999, OMHAR sent a letter to 11 nonpublic entities to notify them that they were qualified to participate in the program. OMHAR requested additional information from these 11 entities and received responses from 8 of them.</p>
Enter into portfolio-restructuring agreements with the participating administrative entities.	To establish the obligations and requirements of the participating administrative entities (§513(a)(2)) and to clarify the duties that they will typically perform.	<p>Not completed. According to OMHAR officials in September 1998, OMHAR hoped to enter into portfolio-restructuring agreements as soon as possible after the participating administrative entities had been selected. OMHAR consulted with representatives from state and local housing finance agencies to develop the basic portfolio-restructuring agreement, which was sent to each of the 52 qualified public participating administrative entities on April 21, 1999. According to OMHAR officials, negotiations with individual public participating administrative entities over the precise contract terms were time consuming. For example, capacity and compensation issues were difficult to resolve. In addition, OMHAR officials said complex legal issues were encountered under state and federal laws that required extensive legal research and consultation. As of December 13, 1999, OMHAR had signed agreements with 37 public and 3 nonpublic entities.</p>

Continued

**Appendix II
Summary and Status of Seven Key Actions
Needed to Implement the Mark-to-Market
Program**

Action	Purpose	Current status
Conduct technical assistance briefings for the participating administrative entities on the mark-to-market process.	To familiarize the participating administrative entities with the restructuring process and their responsibilities, which include determining the project owner's eligibility, determining the rent levels, restructuring the loans, underwriting new or modified loans, managing the closing process, distributing documents after closing, and servicing the loans.	Completed behind schedule. According to OMHAR officials in September 1998, the briefing sessions for the participating administrative entities were planned to begin in October 1998. However, OMHAR officials said this timetable was revised (after the OMHAR Director was appointed in October 1998) to allow OMHAR time to establish a proper infrastructure to successfully implement the mark-to-market program. Consequently, it was not until mid-January 1999 that a technical briefing session for potential public participating administrative entities was held. The briefing's purpose was to provide a general overview of the mark-to-market program and to solicit comments on an early draft of the portfolio-restructuring agreement. OMHAR's financial advisor developed a plan to conduct technical briefing sessions for the participating administrative entities, OMHAR field office staff, and HUD staff. The first 1-day briefing session (to be conducted with each participating administrative entity as agreements are executed) was held in May 1999, and as of December 1999, 30 additional sessions had been held. The purpose of these sessions is to provide the participating administrative entities with a general overview of the mark-to-market program and their roles and responsibilities.
Develop an operating procedures guide.	To set forth a uniform process for restructuring FHA-insured Section 8 housing projects.	Completed behind schedule. In September 1998, OMHAR officials expected the draft guide to be ready for departmental clearance by mid-September 1998. The guide was not issued, however, until April 19, 1999. According to OMHAR officials, the Office needed to coordinate several key issues and work cooperatively with HUD's offices of Housing and General Counsel since the mark-to-market program significantly impacts HUD's multifamily housing programs. OMHAR also consulted with representatives from state and local housing finance agencies on the development of the operating procedures guide.
Prepare a front-end risk assessment report for the permanent mark-to-market program.	To identify the risks related to fraud, waste, and abuse of federal resources and to document both the existing program controls and management's plans for implementing additional controls to mitigate the identified risks.	Completed behind schedule. In September 1998, OMHAR officials expected the contract to complete the front-end risk assessment to be awarded that month. The report was expected to be completed 60 days later, or about mid-November, 1998. However, the front-end risk assessment report was not completed until July 1999. According to OMHAR officials, competing work priorities resulted in OMHAR's completing the planned action portion of the report later than anticipated. However, they said the report's findings were considered in OMHAR's development of the organization, performance standards for the participating administrative entities, and procurement of contract resources.

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**Appendix II
Summary and Status of Seven Key Actions
Needed to Implement the Mark-to-Market
Program**

Action	Purpose	Current status
Develop an Internet-based tracking system.	To enable OMHAR to monitor actions taken by the participating administrative entities and HUD's field offices in carrying out mark-to-market functions.	Completed behind schedule. In October 1998, OMHAR expected the system to be ready for assigning projects to the participating administrative entities, tracking their fees, and tracking projects under the permanent program by November 1998. However, testing on the system was not completed until April 1999. In May 1999, OMHAR implemented the first release of the system. According to OMHAR officials, the delay in implementing the tracking system did not present a risk to implementing the mark-to-market program because a stand-alone application to identify the projects submitted to OMHAR had been developed prior to implementing the tracking system. Furthermore, OMHAR officials said the implementation of the tracking system coincided with OMHAR's first assignment of projects to the participating administrative entities.

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Note: All section citations refer to P.L. 105-65.

OMHAR's Implementation of Eight Other Key Statutory Requirements

Task	Statutory requirements	OMHAR's planned implementation
Determine market rents.	<p>According to the act (§514(g)(1)), rent levels must either be (1) equivalent to the rents derived from not less than two comparable properties or (2) equal to 90 percent of the fair market rent if comparables are not available. The act (§512(1)) defines comparable properties as properties in the same market areas that are similar to the housing project as to neighborhood, type of location, access, street appeal, age, property size, apartment mix, utilities, and other relevant characteristics and are not receiving project-based assistance. The act (§514(g)(2)) also provides exceptions, whereby rents may exceed market rents, but not exceed 120 percent of the fair market rent. The participating administrative entities may approve exception rents on 20 percent of the units covered by the portfolio-restructuring agreement. The act's accompanying conference report stresses that the participating administrative entities set rents at a reasonable level near or at market rates according to the rents of other comparable properties in the market, not the fair market rent. The conference report also says that the participating administrative entities may approve exception rents to ensure the projects' financial viability. According to the congressional colloquies regarding the mark-to-market program, the legislation was crafted to allow the consideration of rent-stabilized apartments within the definition of comparable properties for the purposes of determining market rent levels.</p>	<p>We found OMHAR's planned implementation of this task to be in accordance with statutory requirements, as follows. According to the regulations (24 C.F.R. 401.410), the restructured rents for project-based assistance must be established at comparable market rents unless the participating administrative entity finds that exception rents are necessary. Comparable market rents are the rents charged for properties that the participating administrative entity determines to be comparable. For purposes of §512(1) of the act, other relevant characteristics include any applicable rent control and other characteristics determined by the participating administrative entity. If the participating administrative entity is unable to identify at least three comparable properties within the local market, the participating administrative entity may use noncomparable housing stock within that market or, if necessary, go outside the market from which adjustments can be made. As a last resort, if the participating administrative entity is unable to identify enough comparable properties, comparable market rents must be set at 90 percent of the fair market rents for the relevant market area. Furthermore, the regulations (24 C.F.R. 401.411) state that exception rents may be provided if the participating administrative entity determines that the project's income under the rent levels established under 24 C.F.R. 401.410 would be inadequate to meet the costs of operating the project and that the housing needs of the tenants and the community could not be adequately addressed. The exception rents are limited to 20 percent of the units covered by the participating administrative entity's portfolio-restructuring agreement. According to the operating procedures guide, the participating administrative entity will discuss the appropriateness of the comparable market rents with the owner, the proposed lender, the physical inspector, and the appraiser after visiting the project and its comparables. Notwithstanding these discussions, the appraiser will make an independent judgment regarding the determination of market comparables.</p>

Continued

**Appendix III
OMHAR's Implementation of Eight Other Key
Statutory Requirements**

Task	Statutory requirements	OMHAR's planned implementation
Renew Section 8 assistance as project-based versus tenant-based.	<p>According to the act (§515(c)(1)), project-based assistance must be renewed if (1) the project is located in an area where available and affordable housing is inadequate, (2) a predominant number of the units in the project are occupied by elderly and/or disabled families, or (3) the project is held by a nonprofit cooperative ownership housing corporation. The conference report mandates the continuance of project-based assistance in tight rental markets. In defining a tight rental market, the conferees believe that a 6-percent vacancy rate is reasonable. For the remaining inventory, the participating administrative entities determine which assistance to provide. Congressional colloquies regarding the mark-to-market program say it is imperative that residents be kept informed of the mortgage-restructuring process and the possibility of receiving tenant-based assistance and be offered ample opportunity to voice their preferences as to the type of assistance provided. The colloquies also state it is not the intent of the drafters of the legislation that HUD attempt to micromanage or second-guess the determination of the participating administrative entity. Neither is it their intent that HUD's regulations include one-sided interpretations of the statutory language, which would force a preference for tenant-based assistance upon the local decisionmakers. The criteria are intentionally objective and neutral, and the final decision for applying them rests at the local level.</p>	<p>We found OMHAR's planned implementation of this task to be in accordance with statutory requirements, as follows. According to the regulations (24 C.F.R. 401.420), the Section 8 contract must be renewed as project-based assistance, subject to the availability of funds for this purpose: if the participating administrative entity determines there is a market-wide vacancy rate of 6 percent or less; if at least 50 percent of the units in the project are occupied by elderly and/or disabled families; or if the project is held by a nonprofit cooperative ownership housing corporation or nonprofit cooperative housing trust. The regulations (24 C.F.R. 401.421) also state, for any project not subject to mandatory project-based assistance under 24 C.F.R. 401.420, the participating administrative entity must develop a rental assistance assessment plan in accordance with section 515(c)(2) of the act to determine whether assistance should be renewed as project-based assistance or whether some or all of the assisted units should be converted to tenant-based assistance. According to the operating procedures guide, mandatory project-based assistance is required for projects (1) in tight rental markets (defined as those with market-wide vacancy rates at 6 percent or below), (2) predominately occupied by elderly or disabled families, or (3) owned by a nonprofit cooperative ownership housing corporation or nonprofit housing trust. The guide also says the participating administrative entity determines whether to renew project-based assistance, provide residents with tenant-based assistance, or renew a portion of the units with project-based assistance and convert the remaining units to tenant-based vouchers. According to the guide, the participating administrative entity makes this decision only after consulting with the affected residents, the project's owner, and local government officials.</p>

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**Appendix III
OMHAR's Implementation of Eight Other Key
Statutory Requirements**

Task	Statutory requirements	OMHAR's planned implementation
Rehabilitate properties.	<p>According to the act (§517(b)(7)) and the conference report, rehabilitation may be paid from the residual receipts, replacement reserves, or any other project accounts not required for the project's operations. Rehabilitation will only be for the purpose of restoring the project to a nonluxury standard adequate for the rental market intended at the original approval of the project-based assistance. Each owner shall contribute, from nonproject resources, not less than 25 percent of the amount of the rehabilitation assistance received.</p>	<p>We found OMHAR's planned implementation of this task to be in accordance with statutory requirements, as follows. According to the regulations (24 C.F.R. 401.452), rehabilitation must be performed to restore the property to the nonluxury standard adequate for the rental market for which the project was originally approved. The regulations (24 C.F.R. 401.472) also state that funding for the rehabilitation must include funds from the project's residual receipts account, surplus cash account, replacement reserve account, and other project accounts, to the extent the participating administrative entity determines that those accounts will not be needed for the initial deposit to the reserves. The owner's contribution requirement will be calculated as 20 percent of the total cost of rehabilitation,³ unless HUD or the participating administrative entity determines that a higher percentage is required. The owner's contribution requirement must include a reasonable proportion (as determined by HUD) of the total cost of rehabilitation from nongovernmental sources. The participating administrative entity may exempt housing cooperatives from the owner's contribution requirement. According to the operating procedures guide, the participating administrative entity's underwriter must confirm that the rehabilitation escrow and reserves for replacement will address the project's 12-month and long-term physical needs. For less than substantial rehabilitation, the rehabilitation escrow should consist of 100 percent of the cost in cash plus 10 percent in either cash or a letter of credit. The underwriter must confirm the amount and the source of the owner's contribution of nonproject funds to the rehabilitation escrow. All owners, except for nonprofit cooperatives, are required to contribute at least 20 percent of the escrow amount. In addition, 3 percent of the rehabilitation cost must come from nongovernmental sources.</p>
Obtain expertise at OMHAR.	<p>According to the act (§574), the Director may appoint and fix the compensation of such officers and employees of the Office as the Director considers necessary to carry out the functions of the Director and the Office. According to the conference report, the conferees intend that OMHAR be staffed with expert employees and have access to private expertise to accomplish the purposes of the act.</p>	<p>We found OMHAR's staffing plans to be in accordance with statutory requirements, as follows. For fiscal year 1999, OMHAR's compensation structure reflected an approximately 19-percent increase over the salary levels for other HUD employees, with a salary cap of \$136,700. See previous section on OMHAR's organization and staffing plans for additional details on OMHAR's hiring.</p>

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**Appendix III
OMHAR's Implementation of Eight Other Key
Statutory Requirements**

Task	Statutory requirements	OMHAR's planned implementation
Disqualify properties.	<p>According to the act (§516), the Secretary may elect not to consider any project's restructuring plan if HUD or the participating administrative entity determines that an owner has engaged in material adverse financial or managerial actions or omissions with regard to such project or the poor condition of the project cannot be remedied in a cost-effective manner. According to the conference report, the participating administrative entity is required to carefully evaluate the project owner's record in operating the property and the property's physical condition. This is the federal government's opportunity to rid the inventory of bad project owners and properties. HUD is authorized to deal with a disqualified property in several ways, including selling or transferring the property to a qualified purchaser. According to the congressional colloquies, it is important for the federal government to terminate its relationship with those owners who have abused the Section 8 program and those properties that are simply unfeasible to continue to subsidize. The colloquies also state that the Secretary of HUD should not only explore the use of sales or transfers to nonprofit organizations but also allow these properties to retain project-based assistance if the ownership or physical condition problems are adequately addressed.</p>	<p>We found OMHAR's planned implementation of this task to be in accordance with statutory requirements, as follows. According to the regulations (24 C.F.R. 401.101), the request of an owner of an eligible project for a restructuring plan will not be considered if the owner or an affiliate is debarred or suspended under part 24 of this title, unless the sale or the transfer of the property is proposed. HUD may also decide not to accept a request for a restructuring plan if HUD notifies the owner that HUD is engaged in a pending enforcement action against that owner or affiliate. According to the operating procedures guide, the participating administrative entity is responsible for making a complete and ongoing assessment of the eligibility of the owner and the project while developing the restructuring plan. If, at any time, the participating administrative entity discovers any grounds for rejection, it must advise OMHAR's field office immediately, provide supporting documentation, and make a recommendation to reject the owner or the project for restructuring.</p>

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**Appendix III
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Task	Statutory requirements	OMHAR's planned implementation
Avoid conflicts of interest and prohibit equity sharing.	According to the act (§513(b)(7)(B)), no private entity shall share, participate in, or otherwise benefit from any equity created, received, or restructured as a result of a portfolio-restructuring agreement. The act (§517(d),(e)) also prohibits HUD from participating in any equity agreement or profit-sharing agreement in conjunction with any housing project under the program and allows HUD to establish guidelines to prevent conflicts of interest under the program. According to the conference report, the prohibitions on equity sharing were mandated because of concerns that equity-sharing arrangements might skew the motivations of the participating administrative entities or HUD in ways counter to the public interest. According to the congressional colloquies, the Senators expected the Secretary to establish strict and coherent guidelines to ensure that the participating administrative entities do not go beyond their restructuring duties as intended under the bill.	We found OMHAR's planned implementation of this task to be in accordance with statutory requirements, as follows. According to the regulations (24 C.F.R. 401.310), the participating administrative entity may not permit conflicts of interest to exist without obtaining a waiver. The participating administrative entity must establish procedures to identify conflicts of interest and to help ensure that conflicts of interest do not arise or continue. HUD will not enter into a portfolio-restructuring agreement with a potential entity that has conflicts of interest or permit one with a conflict to continue performance under an existing portfolio-restructuring agreement. The participating administrative entity has a continuing obligation to take all necessary actions to identify whether it has a conflict of interest. The regulations (24 C.F.R. 401.311) also state that, in connection with the performance of any portfolio-restructuring agreement and during the term of such agreement, a participating administrative entity or other restricted person may not (1) solicit for itself or others favors, gifts, or other items of monetary value from any person who is seeking official action from HUD or the participating administrative entity in connection with the agreement or has interests that may be substantially affected by the restricted person's performance or nonperformance of duties to HUD; or (2) improperly use HUD's property or property over which the restricted person has supervision or charge by reason of the agreement; or (3) use its status as the participating administrative entity for its own benefit, or the financial or business benefit of a third party, except as contemplated by the agreement; or (4) make any unauthorized promise or commitment on behalf of HUD. According to the operating procedures guide, both the owner and the participating administrative entity are responsible for notifying OMHAR headquarters of any potential conflicts of interest that may exist for either party during the restructuring process.

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Task	Statutory requirements	OMHAR's planned implementation
Obtain tenant participation.	<p>According to the act (§514(f)), the HUD Secretary must establish procedures to provide an opportunity for the project's tenants and other affected parties to participate effectively and on a timely basis in the restructuring process. These procedures must take into account the need to provide the project's tenants and other affected parties timely notice of proposed restructuring actions and appropriate access to relevant information about restructuring activities. The procedures must give all such parties an opportunity to provide comments to the participating administrative entity in writing, in meetings, or in another appropriate manner. According to the congressional colloquies regarding the mark-to-market program, the Congress fully expects that the participating administrative entities will establish procedures that ensure meaningful and effective participation for residents of the restructured projects and other affected parties. The colloquies also state that the Senators expect the participating administrative entities to take this concern seriously, while balancing it with the need to complete the restructuring process in a timely fashion.</p>	<p>We found OMHAR's planned implementation of this task to be in accordance with statutory requirements, as follows. According to the regulations (24 C.F.R. 401.500), the participating administrative entity must solicit and document the consideration of the tenants' comments. At a minimum, three notices must be provided. The first is a notice of intent to restructure, which must include the project, the responsible participating administrative entity and the contact person, the owner's notice of intent to restructure through the mark-to-market program, and the expiration date of the project-based assistance. The second is a notice that includes the location of the restructuring plan for inspection and copying and the date, the time, and the place of the public meeting. The third is a notice of the completion of the restructuring plan. This notice must describe the completed restructuring plan and restructuring commitment or the reasons not to restructure. In addition to the regulations, the operating procedures guide includes detailed requirements relating to the tenants' participation. Among other things, the procedures include requirements for the participating administrative entities to (1) notify the tenants of mark-to-market activities; (2) obtain and document their comments submitted in response to the notices; (3) conduct a meeting to hear presentations and comments on the desired contents of the restructuring plan, on the owner's evaluation of the project's physical condition, and on any proposed transfer of the project; (4) conduct a follow-up meeting with the tenants and other affected parties to provide them with the opportunity to offer additional input on the restructuring plan; (5) make the completed restructuring plan available for inspection by the tenants; and (6) provide the tenants and the community with access to various documents relating to the restructuring process.</p>
Collect public comments.	<p>According to the act (§522), the Secretary must seek recommendations regarding the selection of the participating administrative entities and the mandatory renewal of project-based assistance for certain Section 8 contracts from affected parties.^b The Secretary must convene three public forums at which the organizations making recommendations may express their views concerning the proposed disposition of the recommendations. According to the act's accompanying conference report, the conferees included special requirements for the Department to seek comment through the public forums in order to focus attention on those issues. The conferees urged HUD to use the forums to elicit a wide range of concerns and recommendations from affected parties.</p>	<p>We found OMHAR's implementation of this task to be in accordance with statutory requirements, as follows. On October 1, 1998, HUD conducted public forums in New York, Chicago, and San Francisco. Forum participants representing a variety of interests made presentations that expanded and clarified written comments on the Department's implementation of the mark-to-market program. In addition to these public forums, OMHAR convened a focus group on November 18, 1998, in Washington, D.C.</p>

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Note: The section citations for the regulations refer to the draft final regulations, dated April 9, 1999.

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^aThe statutory requirements and the regulations for an owner's contribution requirement are mathematically equivalent. In other words, 25 percent of the amount of rehabilitation assistance an owner receives equates to 20 percent of the total rehabilitation costs.

^bAffected parties may include organizations representing state and local housing finance agencies, other potential participating administrative entities, tenants, owners, and managers of eligible multifamily housing projects, states, units of general local government, and qualified mortgagees.

Comments From the Department of Housing and Urban Development



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

December 13, 1999

Ms. Judy A. England-Joseph
Director, Housing and Community
Development Issues
United States General
Accounting Office
Washington, DC 20548

Dear Ms. England-Joseph:

The following is in response to your November 23, 1999, letter which solicited the Department's comments on your Office's draft proposed report titled "HUD's Restructuring Office's Actions to Implement the Mark-to-Market Program" (GAO/RCED-00-21).

I would like to express my appreciation for the opportunity to review and comment on your Office's draft report summarizing the steps that the Office of Multifamily Housing Assistance Restructuring (OMHAR) has taken to implement the Mark-to-Market (M2M) Program and "The Multifamily Assisted Housing Reform and Affordability Act of 1997 (MAHRA)." We commend your staff on the quality and the depth of the questions raised during the course of their review. We also appreciate their professionalism in handling some of the sensitive and controversial issues that have arisen during the course of their review.

We understand the process of how a report gets initiated within GAO; and while we further understand the priority that GAO gives to requestors in determining the scope of an evaluation, we do have concerns that this process necessarily precludes a fully balanced picture from being achieved.

Secondly, OMHAR was thorough in its analysis of pricing for the Participating Administrative Entities (PAEs). Our original estimate was that the proper fee should be between \$25,000 and \$30,000. At that time, the states asked for a fee of \$35,000, which was granted to them in an effort to honor the legislative mandate. Notwithstanding concessions made by OMHAR, as is indicated in your report, some of the states still believe our fee is not reasonable. However, we now have two sets of contracts to demonstrate the accuracy of our initial estimate. Our first contracts with private PAEs, including one nonprofit, averaged \$26,166. The second averaged \$26,860. In other words, the preference came at a price. While we believed it was necessary to honor the statute's preference provision, it was also necessary to honor its cost-effectiveness provision as well. It has come to our attention that for some agencies, pricing is still an issue due to the costs that they expect to incur in subcontracting out a significant portion of their M2M restructuring activities.

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Lastly, while the report implies that OMHAR's delay in signing contracts with the public PAEs caused delay in the program's implementation, the real question is whether it was done right. OMHAR conducted negotiated discussions with PAEs and their trade groups to develop standardized contract provisions, and to take account of their concerns early in the process. We have continued to honor the congressional priority for entering into contracts with PAEs which, as noted above, has come at a cost. However, we are only one party to the contract. While we have been ready and willing to sign contracts since early this year, we cannot force the pen of another party. Moreover, we took Congress' will of cost-effectiveness and oversight quite seriously. To lower these standards would have caused long term damage to assisted housing.

While we understand that the purpose of this report is to respond to specific questions/issues, we would like to request that any further review of OMHAR and it's implementation of the M2M Program be expanded to more accurately portray the complex issues and conflicting goals that OMHAR has had to balance.

As you may know from your staff's review of the M2M Program, OMHAR has made significant strides in implementing the Program since your Office's initial report, which was issued in October 1998 (GAO/RCED-99-5). During the past year, OMHAR has:

- established office space for an OMHAR Headquarters and four Regional Office locations,
- signed the final regulations into clearance,
- filled or selected 87percent of the 75 FTE positions authorized for OMHAR for Fiscal Year 1999,
- qualified 52 public state and local housing finance agencies and 11 nonpublic entities to serve as PAEs,
- procured Financial Advisory and Technical Support Services using the GSA Schedule with a team of that includes some of the leading experts in the areas of affordable housing, FHA multifamily insured programs and Federal Credit Reform,
- conducted several input sessions with a NCSHA working group to discuss the M2M Operating Procedures Guide (OPG) and Portfolio Restructuring Agreement (PRA),
- issued a M2M Program Operating Procedures Guide,
- finalized the Portfolio Restructuring Agreement (PRA),
- executed PRAs with 37 qualified public PAEs and three nonpublic PAEs,
- provided 30 relationship building sessions to 40 PAEs,
- provided 5 in-depth underwriting sessions to signed PAEs,
- conducted a Front End Risk Analysis of the Program,
- participated in various training and briefing sessions with Housing and Community Builder staff,
- developed PAE performance measures,
- implemented M2M Management Information System, which includes among other things, a tracking system,
- drafting an internal staff procedures guide,
- developing a comprehensive oversight and audit plan,
- developed streamlined processes with various other offices within HUD which provide support services to OMHAR; and
- providing support to the Office of Housing to close Demonstration pipeline deals.

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While OMHAR has accomplished many actions, we recognize that there were several actions that were completed behind overly aggressive internally projected time frames. Many of these delays, in large part, were due to the challenge that OMHAR faced in starting up a new organization in the existing structure of the Federal government, while also developing the mechanisms for contracting, managing and overseeing the PAEs. To address this challenge, OMHAR officials researched other Federal programs, e.g. coinsurance and FNMA Delegated Underwriting and Servicing, similar to this and concluded that the most important step we could take was to ensure that the proper protocols were established at the beginning of the program rather than rushing to do deals without the proper infrastructure and guidelines in place.

While OMHAR and the Department are very pleased with the progress made to date in the implementation of the M2M Program, we recognize that the future brings even greater challenges to OMHAR. With over 1,000 deals in the M2M pipeline, of which almost 700 have been assigned to PAEs or are awaiting PAE acceptance, OMHAR is officially open for business and will face a whole new set of issues. We are confident that the extra time spent in setting up the proper infrastructure and protocols will allow us to more efficiently respond to the issues that will arise in this stage of program implementation.

Based on our review of the Draft Report to Congressional Committees on OMHAR's actions to implement the M2M Program, we believe that your staff has accurately described the Department's efforts to date in implementing M2M Program and MAHRA. While we agree that the report is accurate in most material matters, we have the following comments:

Now on p. 12.

1. Page 9 and 10, Footnote 9. This may be made clearer by indicating that the legislative post-employment provisions will apply to only those OMHAR employees whose base salary exceeds the highest level of a GS-15.

Now on p. 12.

2. Page 10, Footnotes 10 and 11. We recommend that these two footnotes be incorporated in the body of the text. Also, it should be noted that the OMHAR Director decided to primarily use competitive hiring procedures for personnel actions so that the process could withstand public scrutiny and avoid any charge of politicization.

Now on p. 13.

3. Page 11, last paragraph. While public announcement of the qualified public PAEs was not made until January 21, 1999, most of the groups were notified of that they were qualified conditioned on the acceptance of OMHAR's fee structure, which at that time was \$30,000, in early October 1999 (copy of a sample letter is enclosed.) However, there were several public PAEs whose proposals were rejected in the first phase and who were permitted by OMHAR, in accordance with the RFQ, to revise and resubmit their proposals for reconsideration. OMHAR staff worked closely with these groups in an effort to qualify them in an effort to comply with the legislative preference for public agencies. Any delay by OMHAR in qualifying all public PAEs was solely attributable to complying with the legislative preference. The Department's public announcement of all qualified groups was withheld until the second phase of review was completed.

Now on pp. 16-17.

4. Page 14, Footnote 17. It is requested that this footnote be incorporated in the body of the text. Also, it should be noted that while OMHAR made the decision to increase the uniform base fee for public PAEs from \$30,000 to \$35,000, the average bid received by the nonpublic PAEs supported the results of the due diligence conducted by OMHAR.

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Now on p. 18.

5. Page 16, Footnote 20. It is requested that the footnote be incorporated into the body of the text. As of December 3, 1999, OMHAR has assigned a total of 536 properties to PAEs. Four hundred sixteen (416) have been assigned to public PAEs and 120 have been assigned to nonpublic PAEs. An additional, 146 assets are awaiting PAE acceptance.

Now on pp. 22-23.

6. Page 20, HUD Support to OMHAR. To clarify the support being provided by HUD's Office of Procurement and Contracts, we recommend the following change to the third sentence in this paragraph:

"In addition, HUD's Office of Procurement and Contracts supports OMHAR by fulfilling the Office's contracting needs, including hiring, at OMHAR's request, a staff person to work primarily on OMHAR's contracting activities. While this individual receives other assignments from OPC, it is expected that OMHAR's needs will take priority."

Should you have any additional questions pertaining to this report, please do not hesitate to call Genevieve Tucker at (202) 708-3856, ext. 3754. We look forward to working with you and your staff in the future.

Sincerely,



Ira G. Peppercorn
Director
Office of Multifamily Housing
Assistance Restructuring

Objectives, Scope, and Methodology

Section 577 of the departments of Veterans Affairs and Housing and Urban Development and the Independent Agencies Appropriations Act of 1998 (P.L. 105-65) requires us to audit the operations of OMHAR annually for the first 2 fiscal years following the date of enactment (October 27, 1997). For this report, our work focused on the status of OMHAR's development by providing information on the Office's (1) progress in obtaining staffing resources, (2) actions to implement the mark-to-market program, (3) implementation of the act's statutory requirements, and (4) relationship with other offices within HUD.

To assess OMHAR's progress in obtaining staffing resources to implement the mark-to-market program, we reviewed the analyses OMHAR completed to develop and finalize its organizational structure and staffing plans. We obtained documentation indicating current and projected staffing levels at OMHAR headquarters and at its four field offices, as well as salary levels for the positions at each of these locations. We interviewed OMHAR and HUD officials to discuss their efforts to hire the staff necessary to carry out the Office's operations and to obtain their views on any barriers to hiring qualified staff. We also reviewed the evaluation by an OMHAR contractor of the Office's staffing issues in a May 14, 1999, front-end risk assessment report on the mark-to-market program.

To provide information on the status of OMHAR's progress on seven key actions that are integral to the program's successful implementation (such as conducting technical assistance briefings on the mark-to-market process and developing an internet-based tracking system), we interviewed OMHAR officials and reviewed relevant documentation to assess the steps OMHAR has taken to implement them. We examined documentation indicating the process that OMHAR followed to qualify public and nonpublic entities for selection to become participating administrative entities and reviewed agreements between OMHAR and these entities. We discussed OMHAR's contract negotiations with four public participating administrative entities that had signed portfolio-restructuring agreements and three entities that were still negotiating with OMHAR as of September 1, 1999, as well as with three entities that had been qualified but later elected to not participate in the program. In addition, we discussed OMHAR's implementation efforts to sign public entities with the National Council of State Housing Agencies (NCSHA) and the Association of Local Housing Finance Agencies.

To determine whether OMHAR has implemented the mark-to-market program in accordance with the act's requirements, we reviewed OMHAR's

planned procedures for nine statutory requirements. We selected these requirements because they were discussed not only in the act but also highlighted in congressional debate and the act's accompanying conference report. We reviewed the act, the conference report, and the debate to determine how OMHAR was to implement the nine requirements. We examined OMHAR's implementation of the requirements by reviewing the mark-to-market regulations, OMHAR's operating procedures guide, and the actions OMHAR has taken to implement the requirements.

To provide information on OMHAR's relationship with other offices within HUD, we interviewed OMHAR and HUD officials to determine the extent of involvement by HUD management in three OMHAR tasks—developing program regulations, a Request for Qualifications for participating administrative entities, and an operating procedures guide for the program. We selected these tasks because they were critical to implementing the mark-to-market program. We reviewed documentation to determine the level and the type of involvement by other HUD offices in each of these tasks. This documentation identified the dates that proposals were submitted to those offices for review, the dates the reviews were completed, the issues raised by those offices during their reviews, and the resolution of those issues. In reviewing this documentation, we also were alert for situations that might indicate that the HUD Secretary had interfered with the OMHAR Director's ability to administer the mark-to-market program. We also interviewed the OMHAR Director to determine if there had been any instance of such interference by the HUD Secretary. In addition, we discussed with OMHAR and HUD officials the types and the amount of support provided by HUD to determine if OMHAR had received adequate support.

GAO Contacts and Staff Acknowledgments

GAO Contacts

Stanley J. Czerwinski (202) 512-7631

Richard A. Hale (202) 512-3090

Acknowledgments

In addition to those named above, John T. McGrail, Andy C. Clinton, Sally S. Moino, and Leigh K. Ward made key contributions to this report.

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