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# ELDERLY HOUSING

# Project Funding and Other Factors Delay Assistance to Needy Households

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# Highlights

Highlights of GAO-03-807T, a testimony before the Special Committee on Aging, U.S. Senate

## Why GAO Did This Study


In 2001, an estimated 2 million elderly households with very low incomes (50 percent or less of area median income) did not receive housing assistance. The Department of Housing and Urban Development (HUD) considered most of these households to be "rent burdened" because they spent more than 30 percent of their incomes on rent. The Section 202 Supportive Housing for the Elderly Program provides capital advances (grants) to nonprofit organizations to develop affordable rental housing exclusively for these households. Based on a report issued in May 2003, this testimony discusses the role of the Section 202 program in addressing the need for affordable elderly housing and factors affecting the timeliness of approving and constructing new projects.


## What GAO Recommends

In its report, GAO made recommendations designed to reduce the time required for projects to receive approval from HUD to start construction. Specifically, GAO recommended that HUD assess the effectiveness of the methods it uses to calculate the size of the Section 202 capital advances and make any appropriate changes to them. GAO also made other recommendations to improve HUD's administration and oversight of the 202 program's performance.

HUD concurred with the recommendations.

www.gao.gov/cgi-bin/getrpt?GAO-03-807T.

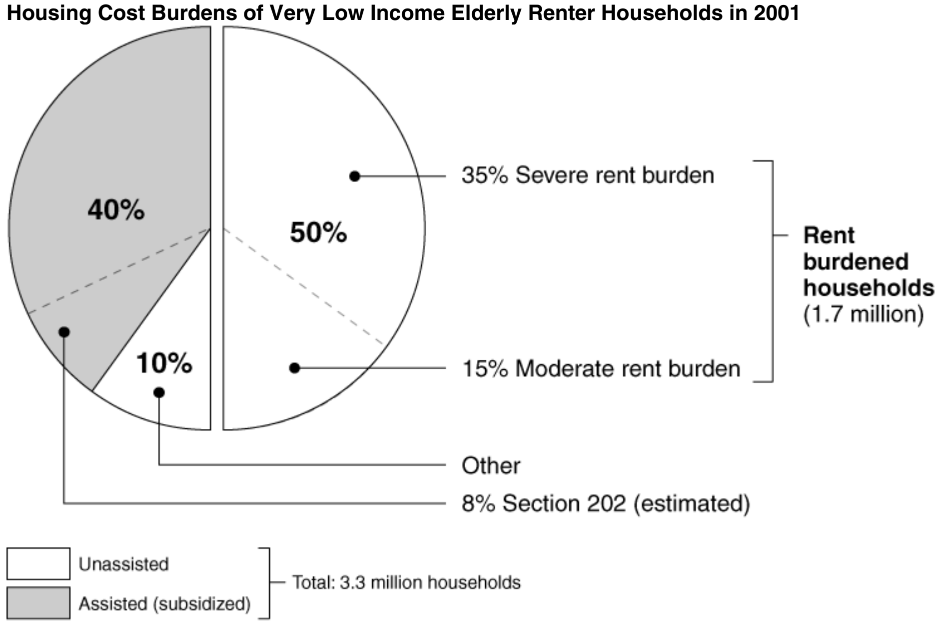
To view the full product, including the scope and methodology, click on the link above. For more information, contact David G. Wood at (202) 512-8678 or WoodD@gao.gov.

## What GAO Found

As the only federal housing program that targets all of its rental units to very low income elderly households, HUD's Section 202 program provides a valuable housing resource for these households. Although they represent a small share of all elderly households, very low income elderly renters have acute housing affordability problems because of their limited incomes and need for supportive services. The Section 202 program offers about 260,000 rental units nationwide and ensures that residents receive rental assistance and access to services that promote independent living. However, even with the program's exclusive focus, Section 202 has only reached an estimated 8 percent of very low income elderly households.

More than 70 percent of Section 202 projects in GAO's analysis did not meet HUD's time guideline for gaining approval to start construction. These delays held up the delivery of housing assistance to needy elderly households by nearly a year compared with projects that met HUD's guideline. Several factors contributed to these delays, particularly capital advances that were not sufficient to cover development costs. Project sponsors reported that because of insufficient capital advances, they often had to spend time seeking additional funds from HUD and other sources. Although HUD's policy is to provide sufficient funding to cover the cost of constructing a modestly designed project, HUD has acknowledged that its capital advances for the Section 202 program sometimes fall short. Other factors affecting the timeliness of the approval process include inadequate training and guidance for field staff responsible for the approval process, inexperienced project sponsors, and local zoning and permit requirements.

**Housing Cost Burdens of Very Low Income Elderly Renter Households in 2001**




Sources: GAO analysis of the American Housing Survey, 2001, and HUD program data.

Mr. Chairman and Members of the Committee:

I appreciate the opportunity to be here today to discuss the Department of Housing and Urban Development's (HUD's) Section 202 Supportive Housing for the Elderly Program. The Section 202 program provides funds to nonprofit organizations to develop affordable rental housing exclusively for very low income elderly households that do not receive other forms of housing assistance. In 2001, there were an estimated 2 million such households in the nation, most of which HUD considered "rent burdened" because their rents exceeded 30 percent of their household incomes.

Section 202 provides two types of financial support. First, HUD provides a project sponsor with a capital advance—essentially a grant—to cover land and construction costs. HUD's policy is to have the capital advance cover the total development costs of the project, which must be of modest design and must comply with HUD's minimum property standards. HUD uses a competitive process to select projects for funding and has guidelines calling for project sponsors and the agency's field offices to accomplish project processing activities—such as completing and approving design plans—within 18 months so that construction may commence. (HUD's field offices may grant extensions of up to 6 months without headquarters' approval.) Second, after the project is completed, HUD provides the sponsor with monthly rental assistance payments to defray some of the operating expenses. For fiscal year 2002, Congress appropriated about $783 million for the Section 202 program to fund the construction of over 6,000 new units, multiyear rental assistance contracts, and other authorized activities.

My statement today is based on the report on the Section 202 program that you requested and are releasing today.[1] Specifically, my statement discusses: (1) the role of the Section 202 program in meeting the housing needs of elderly renter households with very low incomes, (2) the extent to which Section 202 projects meet HUD's time guideline for approving projects to start construction, and (3) the factors that keep Section 202 projects from meeting the time guideline. In preparing the report, we analyzed data from HUD and other sources on the housing needs of very low income elderly households. In addition, we reviewed HUD program and budget data, surveyed all 45 HUD field offices that process Section 202

[1] *Elderly Housing: Project Funding and Other Factors Delay Assistance to Needy Households*, May 30, 2003 (GAO-03-512).

projects, and surveyed and interviewed project sponsors and consultants experienced in working with the Section 202 program. Our analysis focused on Section 202 projects funded between fiscal years 1998 and 2000.[2]

In summary:

- As the only federal housing program that targets all of its rental units to very low income elderly households, Section 202 is an important source of affordable housing for these households. Section 202 insulates tenants in housing units subsidized by the program from increases in housing costs by limiting their rents to 30 percent of household income. As of 2001, the program provided housing for an estimated one-fifth of the 1.3 million elderly renter households with very low incomes that received some form of government housing assistance. However, nationwide about 1.7 million elderly renter households with very low incomes did not receive government housing assistance and had a housing affordability problem—that is, they paid over 30 percent of their incomes for rent. Even with the program's exclusive focus, Section 202 has only reached an estimated 8 percent of very low income elderly renter households.

- More than 70 percent of Section 202 projects funded between 1998 and 2000 were delayed—that is, they took longer than the 18 months set out in HUD's guidelines to proceed from the date of the funding award to the date of HUD's approval to start construction (the project processing period). However, a majority of projects were approved for construction within 24 months, or 18 months plus the 6-month discretionary extension. Projects located in metropolitan areas were more likely than projects in nonmetropolitan areas to exceed the 18-month guideline. Further, projects that exceeded the 18-month guideline ultimately took an average of 11 months longer to finish than projects that met the time guideline, and these delayed projects contributed to the program's unexpended fund balances. At the end of fiscal year 2002, 14 percent of the Section 202 program's $5.2 billion in unexpended appropriations was associated with projects that had not yet been approved for start of construction after 18 months.

- Several factors impeded the timely processing of projects, according to project sponsors, consultants, and HUD field office staff. First, despite

[2]Lack of reliable program data prevented us from reviewing all Section 202 projects funded before fiscal year 1998.

HUD's intent, capital advances have not always covered the cost of developing projects, and the resulting shortfalls often prolonged processing times, in part because sponsors needed to seek additional funding. Second, field office staff's inconsistent implementation of procedures intended to streamline processing, as well as limited training and out-of-date guidance on processing policies and procedures, impeded timely processing. Third, HUD's project monitoring system has limitations that may have hindered HUD's ability to oversee project timeliness. Finally, other factors—including inexperienced sponsors and local permit and zoning requirements—prolonged processing time for some projects.

Based on our findings, we recommended that HUD evaluate the effectiveness of the current methods for calculating capital advances and make any changes necessary to ensure that capital advances adequately cover development costs. We made three additional recommendations—concerning HUD's training of field office staff, handbook guidance, and data systems—directed at more timely processing of projects. In commenting on the report, HUD agreed with the recommendations.

## Background

HUD defines elderly households as those in which the householder—the person whose name is on the lease, mortgage, or deed—or the householder's spouse is at least 62 years old. Elderly households occupied about one-quarter (26 million) of the approximately 106 million housing units in the United States in 2001, according to the American Housing Survey.[3] A large majority of these elderly households were homeowners. A small share of elderly households, about 19 percent or 5 million, rented their homes (compared to about 36 percent of nonelderly households), and about 3.3 million of these elderly households were renters with very low incomes—that is, 50 percent or less of area median income.

The Housing Act of 1959 (P.L. 86-372) established the Section 202 program, which began as a direct loan program that provided below-market interest rate loans to private nonprofit developers, among others, to build rental housing for the elderly and people with disabilities. In 1990, the Cranston-Gonzalez National Affordable Housing Act (P.L. 101-625) modified Section

[3]As in other surveys, estimates from the American Housing Survey are subject to both sampling and nonsampling errors. All numerical estimates derived from the survey have sampling errors of ±10 percent or less of the value of those numerical estimates, unless otherwise noted. All percentage estimates have sampling errors of ±6 percentage points or less, unless otherwise noted.

202 by converting it from a direct loan program to a capital advance program.

In its current form, Section 202 provides capital advances—effectively grants—to private nonprofit organizations (usually referred to as sponsors or owners) to pay for the costs of developing elderly rental housing. As long as rents on the units remain within the program's guidelines for at least 40 years, the sponsor does not have to pay back the capital advance. HUD calculates capital advances in accordance with development cost limits that it determines annually, and HUD's policy is that these limits should cover the reasonable and necessary costs of developing a project of modest design that complies with HUD's project design and cost standards as well as meets applicable state and local housing and building codes.

To be eligible to receive Section 202 housing assistance, households must have very low income and one member who is at least 62 years old. Section 202 tenants generally pay 30 percent of their income for rent. Because their rental payments are not sufficient to cover the property's operating costs, the project sponsor receives rental assistance payments from HUD to cover the difference between the property's operating expenses (as approved by HUD) and total tenant rental receipts.[4] In addition, the project sponsor can make appropriate supportive services, such as housekeeping and transportation, available to these elderly households.

From year to year, Section 202 has carried significant balances of unexpended appropriated dollars for capital advances and rental assistance payments. In fiscal year 2002, the unexpended balance for Section 202 was approximately $5.2 billion. About 41 percent of this balance was in capital advance funds and 59 percent was in rental assistance funds. Some of these unexpended funds have not yet been awarded to projects, and others are for projects that have not begun construction. Once construction begins, funds are expended over several years during the construction phase and during the term of the rental assistance contracts.

[4]The term on rental assistance contracts is 5 years, although HUD has authorized these contracts for as long as 20 years. After these contracts expire, HUD renews them for 5 years, subject to the availability of funds.

Other federal programs can provide housing assistance to needy elderly households, albeit not exclusively. For example, low income housing tax credits and tax-exempt multifamily housing bonds provide federal tax incentives for private investment and are often used in conjunction with other federal and state subsidies in the production of new and rehabilitated rental housing. The Housing Choice Voucher Program supplements tenants' rental payments in privately owned, moderately priced apartments chosen by the tenants. Currently, about 260,000 of the approximately 1.5 million voucher households are elderly. Other programs are discussed in an appendix to the report.

## Section 202 Is an Important Source of Housing for Elderly Households with Very Low Incomes

Section 202 is the only federal housing program that targets all of its rental units to very low income elderly households. Because these households often have difficulty affording market rents, program funding is directed to localities based in part on their proportions of elderly renter households that have a housing affordability problem. Section 202 insulates tenants in housing units subsidized by the program from increases in housing costs by limiting rents to a fixed percentage of household income. The program is a significant source of new and affordable housing for very low income elderly households. Even with the program's exclusive focus on the very low income elderly, Section 202 has reached only a small share of eligible households.

### Section 202 Targets Very Low Income Elderly Households and Makes Supportive Services Available

Congress specifically intended the Section 202 program to serve very low income elderly households and to expand the supply of affordable housing that can accommodate the special needs of this group.[5] HUD takes into account the need for the kind of housing Section 202 provides when allocating program funds to the field offices. The criteria for allocating funds to the field offices include, among other things, the total number of very low income elderly renters in the area and the number in this group that pay more than 30 percent of their incomes for rent. According to the American Housing Survey, in 2001 about 1.7 of the 3.3 million elderly renters with very low incomes paid over 30 percent of their incomes for rent.

The rent that tenants in Section 202 housing pay equals a percentage of their household incomes—generally 30 percent. This percentage remains

[5] 12 U.S.C. 1701q(a).

constant, so the amount of rent tenants pay increases only when household income rises, protecting them from rent increases that might be imposed by the private housing market when market conditions change. In contrast, very low income elderly renter households that do not receive this type of assistance are vulnerable to high rent burdens and increases in market rents. Most of these households have few or no financial resources, such as cash savings and other investments, and rely primarily on fixed incomes that may not increase at the same rate as market rents.

Section 202 serves another important function, potentially allowing elderly households to live independently longer by offering tenants a range of services that support independent living—for example, meal services, housekeeping, personal assistance, and transportation. HUD ensures that sponsors have the managerial capacity to assess tenants' needs, coordinate the provision of supportive services, and seek new sources of assistance. HUD pays a small portion of the costs of providing these services through its rental assistance payments.

## Section 202 Provides an Estimated One-Fifth of All Government-Subsidized Housing for Very Low Income Elderly Renters

According to the American Housing Survey, in 2001 about 1.3 million, or 40 percent, of elderly renter households with very low incomes received some form of rental assistance from a government housing program, including Section 202. According to our analysis of HUD program data, about 260,000 Section 202 units with rental assistance generally served very low income elderly households in 2001. Taken together, these two sources of data suggest that Section 202 served around one-fifth of the 1.3 million assisted elderly households identified in the American Housing Survey.[6]

While Section 202 is an important source of affordable elderly housing, the program has reached a relatively small fraction of very low income elderly renter households. Between 1985 and 2001, Section 202 reached no more than about 8 percent of elderly households eligible for assistance under the program. Also, during this period, many of the elderly renter households with very low incomes—ranging from about 45 to 50 percent—had housing affordability problems. Other federal programs that develop rental housing generally target different income levels, serve other populations in addition to the elderly (including families with children and

[6]Because this estimate is derived from two different sources, we cannot give a precise percentage; thus, this estimate is intended to be illustrative.

people with disabilities) and do not require housing providers to offer supportive services for the elderly.

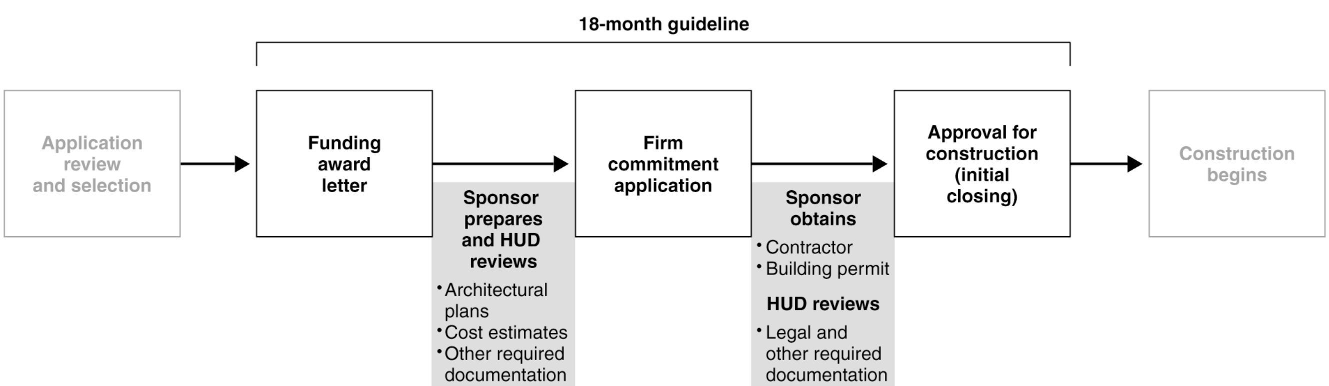
## Section 202 Projects Generally Did Not Meet Guidelines for Timeliness

Most of the Section 202 projects funded between fiscal years 1998 and 2000 did not meet HUD's guideline for approving the start of construction within 18 months. However, a slight majority of the projects were processed and approved to start construction within 24 months. Timeliness varied both across HUD's field offices and by project location (metropolitan versus nonmetropolitan areas). As well as taking longer to complete than other projects and thus delaying benefits to very low income elderly households, projects that were not approved for construction after the 18-month time frame increased the Section 202 program's year-end balances of unexpended appropriations.

### HUD Took Longer Than 18 Months to Approve Most Projects for Construction

HUD's guidelines state that within 18 months of the funding award date, field offices and project sponsors must complete various task before construction can commence (fig.1). Altogether, 73 percent of the Section 202 projects funded from fiscal years 1998 through 2000 did not meet this 18-month processing time guideline. These projects accounted for 79 percent of the nearly $1.9 billion in funding awarded to projects during this period. Also during this period, 78 percent of projects located in metropolitan areas exceeded the 18-month guideline as opposed to 61 percent of projects located in nonmetropolitan areas.

**Figure 1: Section 202 Project Processing**




Source: GAO presentation based on flowchart provided by HUD.

HUD field offices may grant an extension of up to 6 months after the 18-month guideline for projects needing more time to gain approval to start construction, and many projects were approved within that 6-month time frame. Of the projects funded from fiscal years 1998 through 2000, HUD approved 55 percent for construction within 24 months of the funding award—27 percent within 18 months and 28 percent within 19 to 24 months. The remaining 45 percent of projects took longer than 24 months to be approved.

We looked at the performance of HUD's 45 field offices that process Section 202 projects and found that they had varying degrees of success in meeting the 18-month guideline. We evaluated their performance by estimating the percentage of projects approved for construction within 18 months for each field office. Among these offices, the median project approval rate for construction within 18 months was 22 percent, but their performance varied widely. Eight field offices had no projects that met the 18-month guideline, while at one office more than 90 percent of projects met the guideline. Field offices' performance varied by region, with those located in the northeast and west being least likely to approve projects within 18 months of the funding award.

## Delayed Projects Affected the Program's Production Times and Expenditures

Meeting processing time guidelines is important because most of the delays in total production time—that is, the time between funding award and construction completion—stem from the project processing phase. When we compared the average total production times for completed projects that did not meet HUD's 18-month processing guideline and those that did, the delayed projects took 11 months longer than other projects to proceed from funding award to construction completion. Since the average time taken for the construction phase was very similar for all projects, most of the 11-month difference in total production time was attributable to the extra 10 months that delayed projects took to complete the processing phase.

Delayed processing of Section 202 projects also affected the Section 202 program's overall balances of unexpended appropriations. At the end of fiscal year 2002, for example, HUD had a total of $5.2 billion in unexpended Section 202 funds. A relatively small part of these unexpended funds—about 14 percent—was attributable to projects that had not yet been approved to start construction and had exceeded HUD's 18-month processing time guideline. Consequently, none of the funds reserved for these projects had been expended. By contrast, the remaining 86 percent of unexpended funds were associated with projects for which HUD was in the process of expending funds for construction or rental assistance. For example, almost half of the unexpended balances—about

48 percent—resulted from projects that had already been completed but were still drawing down their rental assistance funds as intended under the multiyear project rental assistance contract between HUD and the project sponsor.

## Various Factors Can Delay the Approval of Projects for Construction

Our review of projects funded from fiscal years 1998 through 2000 shows that several factors impeded Section 202 projects from meeting the 18-month processing time guideline, including insufficient capital advances, limited training and guidance for HUD field office staff on processing policies and procedures, and limitations in HUD's project monitoring system. Factors external to HUD, such as sponsors' level of development experience and requirements established by local governments, also hindered processing.

### Insufficient Capital Advances Caused Some Sponsors to Seek Other Funding

Although HUD policy intends for capital advances to fund the cost of constructing a modestly designed project, capital advances have not always been sufficient to cover these expenses.[7] HUD field office staff, project sponsors, and consultants reported that program limits on capital advances often kept projects from meeting HUD's time guideline for approving projects for construction. Most field offices, and every sponsor and consultant that we surveyed, reported that insufficient capital advances negatively affected project processing time, and a substantial majority of respondents indicated that this problem occurred frequently. Many respondents also reported that securing secondary financing to supplement the capital advance amount often added to processing time. According to nearly all sponsors and consultants, the capital advance amounts set by HUD were frequently inadequate to cover land, labor, and construction costs as well as fees imposed by local governments. As a result, sponsors had to seek secondary financing from other federal, state, and local sources—including other HUD programs—or redesign projects to cut costs, or both. According to a HUD official, the agency is currently initiating steps to study the sufficiency of capital advances in covering project development costs.

[7]See 66 *Fed. Reg.* 6647 (Jan. 22, 2001).

## Varying Field Office Practices and Inadequate Staff Training and Guidance Affected Timely Processing

In 1996, to help ensure that field office staff and project sponsors could complete project processing requirements within the 18-month time guideline, HUD adopted changes that were intended to streamline processing procedures.[8] One of the key changes included requiring field office staff to accept sponsor-provided certifications of architectural plans, cost estimates, and land appraisals. Previously, field office staff performed detailed technical reviews of these items.

According to our survey, differences in the procedures field offices used to approve projects for construction and the lack of staff training and experience affected project processing time. For example, most consultants and sponsors in our survey responded that inconsistent implementation of streamlined processing procedures by field offices caused delays, as did insufficient training for and inexperience of field office staff. Some consultants and sponsors whom we interviewed told us that some field offices continued to conduct much more detailed and time-consuming technical reviews of project plans than HUD's current policies require.

HUD has provided limited guidance for field office staff on the current processing policies and procedures. At the time of our review, most field office staff had not received any formal training on Section 202 project processing. According to HUD, in 2002, the agency required representatives from each field office to attend the first formal training on project processing for field office staff since at least 1992. Although HUD headquarters expected those who attended to relay what they had learned to other staff members in their own offices, our survey showed that by November 2002 no on-site training had occurred at about a quarter of the field offices. We also found that HUD's field office staff was relying on out-of-date program handbooks that did not reflect the streamlined processing procedures.

## Administrative and Oversight Weaknesses at HUD Headquarters Contributed to Delays

HUD's project monitoring system was not as effective as it could have been and may have impeded HUD's oversight of project processing. HUD officials told us that headquarters periodically uses its Development Application Processing (DAP) system to identify projects that have exceeded the 18-month processing time guideline. In addition, headquarters contacts field offices on a quarterly basis to discuss the

[8] HUD Notice H 96-102.

status of these delayed projects. Nevertheless, HUD officials have acknowledged that there are data inaccuracies in the DAP system. The lack of reliable, centralized data on the processing of Section 202 projects has limited HUD headquarters' ability to oversee projects' status, determine problematic processing stages, and identify field offices that may need additional assistance. HUD officials indicated that enhancing the DAP system is a priority, but that a lack of funding has hindered such efforts.

Finally, other factors outside of HUD's direct control kept some projects from meeting the time guideline, according to field office representatives and sponsors and consultants responding to our survey. Almost all survey respondents agreed that project processing time was negatively affected when sponsors were inexperienced in project development. Nearly 60 percent of field offices, and almost 40 percent of sponsors and consultants, indicated that this problem occurred frequently. A majority of survey respondents reported that local government permitting and zoning requirements prolonged project processing, although we found differences of opinion on whether these problems occurred frequently. Community opposition and environmental issues were also reported to negatively affect project processing time, but not frequently.

Mr. Chairman, this concludes my prepared statement. I would be happy to answer any questions at this time.

## Contacts and Acknowledgments

For further information on this testimony, please contact David G. Wood at (202) 512-8678 or Paul Schmidt at (312) 220-7681. Individuals making key contributions to this testimony included Emily Chalmers, Mark Egger, Daniel Garcia-Diaz, William Sparling, and Julianne Stephens.