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Final Report

Evaluation of the Rental Rehabilitation Program



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EXECUTIVE SUMMARY

The Rental Rehabilitation Program (RRP) was authorized on November 30, 1983, by Section 301 of the 1983 Housing and Urban-Rural Recovery Act. Congress initially appropriated \$300 million for the program, \$150 million each for FY 1984 and FY 1985, to be distributed on a formula entitlement basis to cities with a population of 50,000 or more, urban counties, consortia of units of general local government, and States for the rehabilitation of privately owned rental housing. In addition, funds were appropriated to provide rental assistance, in the form of Section 8 certificates and housing vouchers, for approximately 60,000 households.

The Rental Rehabilitation Program breaks traditional patterns for lower income housing programs by neither limiting nor guaranteeing the level of project rents, but instead, provides rental assistance payments to lower income tenants who may continue to reside in the reiovated units or move elsewhere. The rehabilitation subsidy to the owner is split from the rental assistance to the tenant. The program is also targeted to a segment of the stock which has received relatively little attention to date: smaller rental properties with moderate repair needs.

This evaluation examined the performance of the program approximately two years after its inception. The study focused on the experience of cities and urban counties, and excluded the State-administered component of the program. It also excluded communities that had not completed a project by the sample selection date (March 31, 1986). The analysis was based on a sample of 35 representative sites and was designed to reflect the way in which the typical grant dollar has been administered.

One community in the sample -- New York City -- has been treated as a separate case study and described in Appendix D. Although it received the largest allocation of program funding (about 11 percent of the national total), New York's program did not reflect the basic RRP model and as a result, was excluded from the core analysis. The findings presented in the body of this report relate to program administration and outcomes in the remaining 34 sites, which included 28 metropolitan cities and six urban counties.

Overview of Program Performance

At the time of the study (July 1986), the median site in the sample had committed 58 percent of its combined FY 1984 and FY 1985 grant allocations, and had expended about 10 percent of those allocations on completed projects. Based on these completions, the Rental Rehab program appeared to be meeting the major performance objectives established by HUD:

- o lower-income households were the primary beneficiaries of the program -- 93 percent had incomes below 80 percent of the area median, and 79 percent of all post-rehab tenants had incomes below 50 percent of the area median;
- o post-rehab rents were generally affordable -- 90 percent of all units had rents that were at or below the applicable Fair Market Rent (FMR);
- o the program was producing a substantial share of larger units -- 80 percent of all completed units had two or more bedrooms, and 20 percent had three or more;
- o the RRP rehab subsidies were relatively low -- \$4,290 for the average unit (\$4,964, including all public subsidy) and;
- o each dollar of RRP rehab subsidy had been matched by \$1.12 of private funds (\$0.92, for all public subsidies).

However, within the study sample, sites exhibited tremendous variation on these and other measures of program performance, and a locality's success (or failure) in meeting one criterion was generally unrelated to its performance with respect to others. This outcome was neither surprising nor inappropriate, given the diversity of local conditions, priorities, and needs.

Program Administration and Design

The Rental Rehabilitation Program was typically administered by a city or county rehabilitation agency working in conjunction with an independent local public housing authority (PHA). City or county actors generally took the lead in designing local programs that meet the RRP objectives and in carrying out most activities related to the selection and rehabilitation of the RRP properties. PHA responsibilities were for the most part restricted to functions related to the issuance of rental assistance payments in the form of Section 8 certificates and vouchers.

There was substantial variation among the sample sites with respect to their previous rehab experience and their approaches to implementing the RRP. However, experience -- both in terms of output under Community Development Block Grant rehab programs and participation in the RRP Demonstration -- was not related to a site's performance under the RRP. Similarly, agency type had little impact on performance.

HUD has encouraged the use of non-repayable rehab subsidies, and half of the sample sites provided grants or forgivable deferred payment loans exclusively. In general, these sites showed higher commitment rates than those offering the subsidy as a repayable loan. Very few sites attempted to

minimize subsidies through the use of gap financing techniques, variable loan terms, or the imposition of a subsidy maximum lower than the 50 percent of cost or \$5,000 per unit cap established by the program.

Despite a strong emphasis in the program statute and regulations on avoiding displacement, relatively few sites actively monitored tenant mobility during the renovation process. The absence of documentation at the local level made the measurement of displacement virtually impossible. Moreover, the sharing of responsibilities for tenant issues between the rehab agency and the PHA sometimes led to misunderstanding about their respective roles and responsibilities.

Program Impact on Tenants

Since most RRP units had rents that were at or below the applicable FMR, they were typically affordable to most households with incomes between 50 and 80 percent of the local median without the provision of rental assistance. However, very low income households generally required Section 8 certificates or housing vouchers to live in RRP units. Eight-two percent of all very low income households received assistance, compared to only 32 percent of all households with incomes between 50 and 80 percent of the local median.

While post-rehab rents varied with market conditions, they were not significantly related to the level of rehab costs, the relative size of the public contribution, or the initial occupancy status of the building. This outcome is consistent with the basic philosophy of the program, which lets the market, and not the government, determine a project's rents.

Program performances measures encouraged the rehabilitation of occupied units. Nevertheless, only about half of all post-rehab tenants had lived in the project prior to rehab. This outcome reflected both the development of vacant properties and the mobility of initial residents. Twenty-eight percent of all pre-rehab tenants moved before the project was complete.

While mobility rates were higher in projects with above-average rent increases, households who moved out of RRP projects tended to have higher incomes than those who stayed or than those who took their place. Such patterns suggest that displacement has not been a significant factor.

Private Sector Response

As intended, the Rental Rehab Program has primarily attracted individual owners of smaller properties with relatively modest renovation needs. The average unit was in a building with four or five apartments, and cost about \$10,000 to rehabilitate. Sixty percent of all units were owned by individuals, with partnerships and trusts the next most common ownership forms (accounting for 17 and 13 percent of the sample, respectively).

Forty-three percent of the cost of the average unit was supported by the RRP grant or loan; another nine percent was funded by other public programs; and the remaining 48 percent was covered by private loans or equity. Units receiving public funding in addition to the RRP contribution had substantially higher rehab costs and substantially lower leveraging ratios.

The decided majority of units would have been unable to support a market rate loan for the full amount of the rehab work. Almost half would have generated a negative cash flow, and about two-thirds would have had cash flow to revenue ratios that were less than 10 percent. However, to retain administrative ease, relatively few sites have attempted to tailor the level of subsidy provided to the individual project's financial needs.

Nature and Cost of Repairs

For the most part, the program has been targeted to properties with relatively modest renovation needs. Roughly 40 percent of all RRP units were rated as in need of limited repairs; 40 percent were dilapidated; and 20 percent were uninhabitable prior to rehab. Rehab costs and the scope of repairs were closely tied to the initial condition of the property.

After rehab, the great majority of projects provided sound, useful housing for people of lower income. The quality of workmanship and materials was rated as "average" in 71 percent of the units; as "high" in 20 percent; and as "poor" in nine percent. Most of the projects with a poor quality rating also appeared to need major repairs at the time of the site visit and would probably fail an HQS inspection.

Allowing local flexibility in determining eligible repairs generally did not result in the use of funds for work other than that necessary to create sound housing for lower-income households. Expenditures to meet HQS and local code requirements averaged \$9,445 per unit, and accounted for 94 percent of total rehab costs. Another five percent was spent on other improvements considered essential to marketability and sound management, and only about one percent went for general property improvements.

Overall Program Performance

Evaluating a program in its initial stages requires some speculation. Furthermore, restricting the sample to sites with completed projects may either overstate or understate the program's accomplishments. Nevertheless, based on the experience of the 34 sites, the Rental Rehab Program appears to be meeting expectations. While initial production has been relatively low, it has accelerated in recent months, and many sites have made adjustments to their programs which should improve performance in this regard. Tenant monitoring needs to be strengthened to insure that displacement does not occur. Nevertheless, the types of households that have been served, the initial affordability of the rehabilitated units, and the completion of appropriate repairs all conformed to established national objectives for the split subsidy approach to rehabilitation of lower income rental property.

CHAPTER 1

INTRODUCTION

The Rental Rehabilitation (RRP) Program was authorized in November, 1983 under the Housing and Urban-Rural Recovery Act of that year. Congress initially appropriated \$300 million for the program, \$150 million each for FY 1984 and FY 1985, to be distributed on an entitlement basis to cities with a population of 50,000 or more, urban counties, consortia of units of general local government, and states for the rehabilitation of privately owned rental housing. In addition, funds were appropriated to provide rental assistance, in the form of Section 8 certificates and housing vouchers, for approximately 60,000 households.

The primary objective of the Rental Rehabilitation program is to increase the supply of safe, decent and affordable housing for low income households through the renovation of the existing stock. As such, it reflects a general shift away from the more expensive new construction programs of the past. The program is also targeted to a segment of the stock which has received less attention under previous rehabilitation programs: smaller rental properties with moderate repair needs. Finally, the program breaks traditional patterns by adopting a "split subsidy" approach. Rehabilitation subsidies are provided to property owners to help support the costs of repairs, but project rents are allowed to rise to their market levels. At the same time, rental assistance is made available to low income tenants who can either remain in the renovated units or move elsewhere.

The design of the Rental Rehabilitation program is intended to allow maximum discretion at the local level. Grantees receive formula allocations of Rental Rehab funds which are then provided to project owners to cover up to half of the cost of rehabilitation or \$5,000 per unit, whichever is less. Grantees choose the form in which the subsidy is offered, identify the neighborhoods in which the program will operate, determine the nature of repairs to be funded, and set the amount of subsidy to be provided to individual property owners. The private market orientation of the program is embodied in the limitation of RRP funds to 50 percent of project costs and the absence of any control on post-rehab rent levels. Significantly, the program relies on the market to set post rehabilitation rents and assumes that proper selection of projects will result in rents that are affordable to low income renters while also yielding an adequate return to property owners.

In order to minimize displacement the RRP also includes a tenant assistance component, consisting of special allocations of Section 8 certificates and housing vouchers. These may be used to assist existing households to remain in their units after rehab or to seek other housing of their choice. Certificates and vouchers may also be offered to new households initially occupying vacant units. However, rental assistance in all cases follows the tenant and is not tied to the rehabilitated unit. Thus, occupancy patterns in RRP projects are determined by market forces, subjecting owners to both the rewards and rigors of the competitive process.

1.1 Purpose of the Evaluation

As the foregoing suggests, the Rental Rehabilitation Program departs in many respects from previous rehabilitation approaches. The purposes of this evaluation are twofold. First, it is intended to assess the extent to which the program is meeting its primary objectives through an examination of the types of properties rehabilitated under the program, the nature of the repairs completed, and the characteristics of the tenants served. Secondly, it is intended to examine local approaches to program operations. While federal regulations establish the basic outline of the RRP, and HUD has developed a number of criteria against which performance could be judged, the success of the program ultimately depends on the ways in which the RRP is designed and implemented at the local level. Thus, the study is intended to describe implementation approaches adopted by local programs and, to the extent possible, identify those features of program administration that contribute to better program performance.

The study employs two basic types of data: program data, describing the RRP programs as they are operating in a sample of 35 cities and counties nationwide, and property level data, describing the characteristics of the projects completed in the sample sites. Program data was collected on-site in each of the 35 sample grantees through administrative interviews with RRP program staff, representatives of participating PHAs, and other actors responsible for the implementation of the program. Interviews were conducted between June and September 1986, after the program had been in operation for approximately two years.

Property level data includes both information on property and tenant characteristics contained in HUD's RRP Cash/Management Information System (C/MI) and supplemental data collected on-site for a sample of 125 RRP properties. These data were collected through a combination of reviews of individual project files, interviews with property owners, and inspections of the completed rental rehab properties. C/MI data reflect outcomes in the 34 sites as of June 1, 1986.

1.2 The Sample

The study focuses on the experience of entitlement grantees, and excludes the state-administered component of the program.¹ A total of 35 different communities were selected for analysis. One of these communities--New York City--has been treated as a separate case study and described in Appendix D. Although it received the largest allocation of program funding (11 percent of the national total) the New York program does not reflect the basic RRP model. The analysis presented here is based on the remaining 34 sites, which includes 28 metropolitan cities and 6 urban counties.

The sample was designed to reflect the way in which the average grant dollar has been administered under the program.² Since a principal objective of the study was to examine program outcomes, we excluded sites that had not yet completed a project at the time that the sample was generated (March 31, 1986). This restriction eliminated 109

1. States have received about 30 percent of RRP funds for reallocation to non-entitlement communities.

2. See Appendix A for a detailed description of the sampling methodology.

out of the 403 entitlement grantees initially participating in the program (excluding New York City), or about 27 percent of all recipients. As a result, the findings presented in this report may be somewhat biased, since the sample excludes some of the least successful sites.

Once the sample was restricted in this manner, the likelihood of selection depended on the size of the site's grant allocation.¹ As noted above, this methodology produces a sample that reflects the way in which the average grant dollar has been administered (excluding sites without completions). While the 34 sites combined represent almost 40 percent of all allocated grant dollars (excluding New York City), they include only about eight percent of all participating communities. As a result, sample averages depict national outcomes, rather than the experience of the average site. Note that the nature of the sampling plan requires weighting the underlying data whenever information on individual sites is combined. When such weights are employed, their use is indicated in a footnote to the charts.

Exhibit 1.1 lists the sites that were included in the study. It also shows the original grant allocation that each received (i.e., FY84 and FY85 combined), as well as any subsequent additions or reductions to those amounts. The initial allocations ranged from a minimum of \$120,600 in Alexandria, Louisiana to a maximum of \$10.7 million in Chicago. Two sites had grants of over \$10 million, 13 sites had grants between \$1 million and \$4 million, 8 sites had grants between

1. Grant allocations refer to combined FY84 and FY85 awards as of March 31, 1986, and reflect any adjustments to the original award amounts that were made prior to that date.

EXHIBIT 1.1

INITIAL AND CURRENT GRANT ALLOCATION OF SAMPLE SITES

	Initial Grant Allocation (FY84 & FY85 Combined)	Revised Grant Allocation (FY 84 & FY85 as of 12/31/86)	Percent Change In Allocation
Chicago, IL	\$10,679,900	\$10,679,900	0%
Los Angeles City, CA	8,612,800	10,752,918	25
Philadelphia, PA	4,706,600	3,606,600	-23
Detroit, MI	3,669,400	2,966,450	-19
Los Angeles County, CA	3,142,000	1,983,000	-37
Houston, TX	2,776,100	3,187,400	15
San Francisco, CA	2,531,100	2,531,100	0
San Diego, CA	1,799,700	1,799,700	0
Newark, NJ	1,631,500	1,631,500	0
Milwaukee, WI	1,540,000	1,631,841	6
Cincinnati, OH	1,447,500	1,447,500	0
Pittsburgh, PA	1,389,700	1,389,700	0
San Antonio, TX	1,326,400	1,546,400	17
Seattle, WA	1,284,500	1,350,192	5
Indianapolis, IN	1,133,000	1,133,000	0
Nassau County, NY	783,800	1,073,800	37
Birmingham, AL	735,100	828,450	13
Toledo, OH	722,700	856,810	19
Tulsa, OK	547,300	277,300	-49
St. Louis County, MO	541,100	541,100	0
New Haven, CN	537,400	668,820	24
Wichita, KS	424,300	214,300	-49
Lexington, KN	408,000	530,400	30
Anaheim, CA	351,000	561,600	60
Anne Arundel County, MD	254,900	254,900	0
Greensboro, NC	247,600	247,600	0
Portland, ME	247,100	247,100	0
St. Clair County, IL	237,600	273,480	15
Rockford, IL	213,800	342,080	60
Islip, NY	199,400	258,200	29
Clackamas County, OR	174,500	174,500	0
Mesa, AZ	161,200	161,200	0
Greenville, SC	150,700	188,700	25
Alexandria, LA	120,600	120,600	0

\$400,000 and \$1 million, and 11 sites had grants that were less than \$400,000.

To promote the expeditious use of program funds, HUD has the authority to reallocate grant awards to increase the funding of good performers and to reduce the funding of recipients that fail to adhere to program guidelines. Adjustments that have occurred to date primarily reflect initial commitment rates.¹ Fifteen of the sample sites have had their original allocations increased as a result of above-average production levels, 5 sites have had monies recaptured, and 14 sites were unaffected. The proportion of sites that have experienced a reduction in funding (15 percent) is below the national rate (21 percent) due to the sample's restriction to communities with at least one completed project.

1.3 Selected Demographic and Market Characteristics of The Sample

The sample communities represent a fairly broad range of market types and conditions that might conceivably affect the operation and effectiveness of the RRP. Exhibit 1.2 presents information on the distribution of sites by size, geographic location, and poverty and mobility rates. Unless otherwise noted, the data were obtained from the 1980 census.

1. In the initial year of the program, the Department reallocated \$2,814,630 of unclaimed FY84 funds to grantees that had committed more than 60 percent of their first year grant amount. Further reallocations and recaptures have been made since that time. In general, HUD has the authority to deobligate grant amounts that have not been committed to specific projects after a two-year period of time. The Department can also deobligate unexpended funds within four years of receipt. Initial program regulations called for the automatic deobligation of funds after the specified time period had expired. However, on August 11, 1986 the Department issued a rule change that allowed case-by-case extensions of up to one year.

EXHIBIT 1.2

SELECTED DEMOGRAPHIC CHARACTERISTICS OF THE SAMPLE¹

	<u>Number of Sites</u>
Community Type	
Central City	26
Suburban City	2
Urban County	6
Geographic Region	
North East	7
South	9
Midwest	10
West	8
Population (1980)	
More than Two Million	3
1,000,000 to 1,999,999	4
500,000 to 999,999	6
250,000 to 499,000	10
100,000 to 249,000	8
Under 100,000	3
Median	370,775
Percent of Households in Poverty (1980)	
< 10 percent	3
10.0 - 14.9 percent	15
15.0 - 19.9 percent	9
20.0 percent or more	7
Median	14.3 percent
Mobility Rates of Renters (1980) ²	
< 30 percent	7
30-39 percent	11
40-49 percent	9
50 percent or more	7
Median	38.8 percent

1. All data were obtained from the 1980 census. Statistics for urban counties exclude entitlement cities within those areas.
2. Defined as percent of renters that had moved into their units within the last year.

Twenty-six of the sample sites are central cities of metropolitan areas, two are cities within the suburban ring, and six sites are urban counties (also located in suburban areas). The sites are distributed fairly evenly across the different geographic regions, and have populations which range from about 50,000 to over 3 million. In the median site, 14 percent of all households had incomes below the official poverty line in 1980, and 39 percent of all renters moved in a given year.

Exhibit 1.3 presents additional information on the characteristics of the housing stock in the sample sites. In the median site, rental units accounted for 49 percent of the housing stock. Eighteen percent of these units were constructed before World War II, and a two-bedroom unit in good condition rented for about \$408 a month (as measured by the most recent FMR). The median rental housing unit cost 22 percent of the median income of renters in 1980. The overall vacancy rate among rental units was 6.5 percent in 1980, and 1.3 percent had been vacant and available for rent for more than 6 months.

While these parameters describe conditions with respect to the median site, the 34 sites show considerable variation along each of the dimensions described above. In an effort to capture this variation and to identify a number of distinct market types, we classified sites according to two important indicators: (1) the cost of rental housing relative to renter income levels (as measured by the ratio of median gross rent to the median income among renters); and (2) the long-term vacancy rate (as measured by the proportion of rental units that have

EXHIBIT 1.3

SELECTED CHARACTERISTICS OF THE HOUSING STOCK
IN THE SAMPLE SITES

	<u>Number of Sites</u>
Percent Renter-Occupied ¹	
< 40 percent	6
40-49 percent	12
50-59 percent	10
60 percent or more	6
Median	49.0 percent
Percent of Rental Units Built Before 1940 ¹	
< 10 percent	9
10-19 percent	10
20-29 percent	10
30 percent or more	5
Median	18 percent
Two Bedroom FMR ²	
\$300-\$399	15
\$400-\$499	11
\$500-\$599	7
\$600 or more	1
Median	\$408
Ratio of Median Gross Rent to Median Income of Renters (1980) ¹	
Under 0.20	6
.20 to 0.24	24
.25 to 0.29	3
.30 or more	1
Median	0.219

1. Data obtained from the 1980 Census.

2. Data reflected to FMR in effect as of 8/86, including any areawide exceptions.

EXHIBIT 1.3

SELECTED CHARACTERISTICS OF THE HOUSING STOCK
 IN THE SAMPLE SITES
 (continued)

	<u>Number of Sites</u>
Percent of Rental Units Vacant ¹	
< 5 percent	7
5.0 to 7.4 percent	15
7.5 to 9.9 percent	9
10.0 or above	3
Median	6.5 percent
Percent of Rental Units Vacant ¹ More Than 6 Months	
< 1 percent	12
1.0 to 1.9 percent	16
2.0 percent or more	6
Median	1.3 percent
Index of Construction Costs ²	
1.10 or more	5
1.00-1.09	5
0.90-0.99	14
0.80-0.89	5
Below 0.80	5
Median	0.96

1. Data obtained from the 1980 Census.

2. Index reflects combined labor and material costs in site in relationship to national average. Locality Adjustments. 1985 Dodge Construction Systems Costs.

been vacant more than 6 months). Sites were assigned to one of four market types based on whether they fell above or below the sample median on each criterion¹. The distribution of sites by this classification is presented in Exhibit 1.4.

Together, the long-term vacancy rate and the rent ratio provide a good picture of rental housing market conditions.² Fourteen of our sites exhibit low rental vacancy rates. In markets of this type, opportunities for investment in the existing stock should be relatively attractive, since owners can be fairly certain of achieving full occupancy. The eleven sites with both low vacancy rates and high rents, in particular, can be characterized as "tight" rental markets. In markets of this type, the incentives for investment in the existing stock should be relatively high, although some owners may conclude that rents are sufficiently high that additional investment is unnecessary.

Twenty of the sites exhibit high long-term vacancy rates among rental units. Generally, high vacancy rates can be expected to discourage investment in the existing stock, particularly when rent levels are low. Eleven sites exhibit both high vacancy rates and low rents, and we characterize these as "loose" markets, where the incentives for investment in the existing housing stock should be particularly weak. Finally, nine sites have both high vacancy rates and

1. Information regarding overall changes in vacancy rates since 1980 was obtained while on site, and appropriate adjustments were made to reflect any adverse or positive trends in the last 6 years.

2. It is important to note that these market indicators refer to the jurisdictions administering the RRP, not to entire metropolitan areas nor to the specific neighborhoods in which the RRP was implemented.

EXHIBIT 1.4

DISTRIBUTION OF SAMPLE SITES BY TYPE OF
RENTAL HOUSING MARKET

<u>Type of Rental Housing Market</u>	<u>Number of Sites</u>
Low Vacancies and High Rents (Tight Markets)	11
Low Vacancies and Low Rents	3
High Vacancies and Low Rents (Loose Markets)	11
High Vacancies and High Rents	9

Note: Sites were classified as high or low based on whether they fell above the sample median for each criterion.

high rents relative to renter incomes. These sites are also likely to have above average poverty rates, and a significant share (6 of the 9) are older, central city jurisdictions. It is difficult to anticipate how the RRP will be received in markets of this type, where high vacancy rates may discourage owner investments even though high rent levels make affordable housing scarce for low income tenants.

1.4 Initial Performance

At the outset, it is important to recognize that this evaluation is being conducted in the initial stages of program development. Unless otherwise noted, all data presented in this report describe the progress of the different sites as of June 1, 1986. As shown in Exhibit 1.5, the sites differ greatly in the extent to which they have committed and expended grant funds under the RRP. Commitment rates based on the site's original FY84 and FY85 grant allocations ranged from 9 to 117 percent, with a median value of 58 percent.¹ Completion rates were considerably lower, ranging from less than one percent to over 75 percent. At the time of our field work, the median site had expended about 10 percent of its allocation on completed projects.²

The numbers of projects and units associated with these commitment and completion rates are presented in Exhibit 1.6. At the

1. Since commitment rates are based on the site's initial grant allocation, and since some sites have received an increase, commitment rates can and do exceed 100 percent.

2. Completion rates are based on projects with complete C/MI cost data. They exclude projects which have obtained their final drawdown, but have not submitted data on actual renovation costs.

EXHIBIT 1.5¹

DISTRIBUTION OF SITES BY PRODUCTION RATES

	<u>Number of Sites</u>
Percent of FY84 and FY85 Grant Funds Committed ²	
Under 20 percent	2
20-39 percent	8
40-59 percent	8
60-79 percent	6
80-99 percent	5
100 percent or more	5
Median	56.5 percent
Percent of FY84 and FY85 Grant Funds Expended on Completed Projects ^{2,3}	
Under One Percent	3
1-9 percent	14
10-19 percent	9
20-29 percent	1
30-39 percent	1
40-49 percent	2
50 percent or more	4
Median	9.6 percent

1. Data obtained from 8/86 C/MI.

2. Commitment and completion rates are based on initial FY84 and FY84 grant allocations.

3. Completion rates are based on projects with complete C/MI cost data. They exclude projects which have obtained their final drawdown, but which have not submitted the final cost data.

EXHIBIT 1.6¹

NUMBER OF PROJECTS AND UNITS PER SITE

<u>I. Commitments</u>	<u>Number of Sites</u>
Number of Projects	
< 10	4
10 - 19	13
20 - 29	7
30 - 39	4
40+	6
Median	19
Number of Units	
< 50	11
50 - 99	7
100 - 199	8
200 - 299	0
300 - 399	3
400 - 499	2
500+	3
Median	88
 <u>II. Completions</u>	
Number of Projects	
One	1
2 - 4	12
5 - 9	10
10 - 19	8
20 or More	3
Median	7
Number of Units	
1-4	2
5 - 9	7
10 - 19	7
20 - 29	6
30 - 49	6
50 or more	6
Median	22

1. Data obtained from 8/86 C/MI.

time that the data were generated, the 34 sites combined had committed funds to 923 projects with 7284 units. A total of 270 projects with 1084 units had been completed. The number of projects completed in a given site ranged from one to 30, while the number of units ranged from 2 to 129. The median site in the sample had completed a total of 7 projects and 22 units. (Unless otherwise noted, most of the data describing units and tenants in this report are based on this sample of completed projects.)

Exhibit 1.7 presents information on the average rehabilitation costs of completed units. Site averages ranged from a low of \$2,477 per unit to a high of \$25,983, with a median of \$8,347. Five sites had average costs below \$5,000 per unit, 16 sites had costs between \$5,000 and \$9,999, 11 sites had costs between \$10,000 and \$19,999, and two sites had costs above \$20,000 per unit. Since the RRP grant cannot exceed \$5,000 per unit, rehab costs in excess of \$10,000 can only be achieved by increasing the private contribution or by supplementing the RRP grant with other public monies.

In addition to production, the Rental Rehabilitation Program attempts to achieve a number of other objectives regarding the types of families served, the affordability of the units produced, the costs to the public sector, and the leveraging of private monies. Six specific performance measures have been developed by HUD to assess a site's performance, and may be used in future years to adjust individual grant allocations.¹ While these measures are by no means definitive, they do

1. A proposed methodology, which was subsequently suspended, appeared in the Federal Register, December 19, 1985, 24 CFR, Part 511.

EXHIBIT 1.7

DISTRIBUTION OF SITES BY AVERAGE
REHABILITATION COSTS PER UNIT¹

	<u>Number of Sites</u>
Under \$5,000 per unit	5
\$5,000 - \$9,999	15
\$10,000 - \$14,999	7
\$15,000 - \$19,999	4
\$20,000 and Above	2
Median	\$8,347 per unit

1. Data obtained from 8/86 C/MI and refer to completed projects only.

provide a useful point of departure for describing the different objectives of the RRP and the performance of sites to date.

The first performance measure reflects the speed with which the site has committed and expended funds, and has already been described and presented in Exhibit 1.5. The five other measures include:

- o the extent to which the rehabilitated units are affordable, as measured by the relationship between project rents and the applicable FMR;
- o the extent to which the RRP is serving larger families, as measured by the proportion of two- and three-or more bedroom units that have been developed under the program;
- o the extent to which the program is serving low income families in substandard housing, as measured by the proportion of post-rehab tenants who have incomes below 50 percent of the area-wide median and who lived in the project prior to rehab;
- o the extent to which the program has minimized public expenditures per unit; and
- o the extent to which the program has maximized the leveraging of private funds.

As noted earlier, this analysis examined the performance of the sample sites when commitment and production rates were relatively low. Rating rental rehab programs at such an early stage in their development is obviously hazardous. Several communities in the sample that had gotten off to a bad start had implemented reforms that are likely to enhance their performance in the upcoming year. In addition, once some on-going construction is complete, the relative performance of a number of sites could change significantly. But despite these important caveats, variations in initial outcomes do reveal some important administrative and market factors that appear to hinder or foster a site's success.

1.4.1 Affordability

Perhaps the most basic principle of the split-subsidy approach is that the units remain affordable to very low income tenants. HUD regulations stipulate that at least 80 percent of the units developed under RRP have gross rents at or below the applicable Fair Market Rent (FMR) for a period of up to seven years. (The FMR represents the cost of a modest unit in standard condition as defined under HUD's Section 8 Existing Housing Program.) The timing of this evaluation obviously precludes us from directly observing success with respect to long-term affordability. However, we can examine the initial affordability of the units developed to date, most of which have been occupied for less than one year.

Exhibit 1.8 shows the distribution of the sample sites by two alternative measures of affordability. At the time of our field work, all but 5 of the 34 sites had met HUD's requirement that at least 80 percent of all units developed under the program have rents at or below the applicable FMR,¹ and in these five sites, the difference between rents and the FMR was relatively small. In 15 sites, one hundred percent of all completed units have met this criterion. While there was not much variation in the proportion of units with rents below the FMR (the performance measure employed by HUD), there was considerable variation in the average ratio of post-rehab rents to the FMR. This

1. These calculations are based on the FMR that was in effect at the time of the project's completion, and include any areawide exceptions.

EXHIBIT 1.8

DISTRIBUTION OF SITES BY POST-REHAB RENTS:
OCCUPIED UNITS ONLY¹

	<u>Number of Sites</u>
Proportion of Units with Rents At or Below FMR	
Less than 80 percent	5
80 to 89 percent	4
90 to 99 percent	10
100 percent	15
Median	0.97
Average Ratio of Rent to FMR	
51-60 percent	1
61-70 percent	1
71-80 percent	6
81-90 percent	9
91-100 percent	15
Over 100 percent	3
Median	0.90

1. Data reflect site averages generated from the 8/86 C/MI, and are based on completed projects only.

ratio ranged from a low of 54 percent to a high of 103 percent, with a median value of 90 percent. Presumably, the lower the ratio, the better the prospects for keeping the units affordable over time.

1.4.2 Focus on Large Units

Another major objective of the RRP is to increase the supply of standard units available to larger families. To accomplish this goal, HUD regulations require that at least 70 percent of all units developed under RRP have two or more bedrooms, although individual sites may seek waivers to reduce this required proportion. A subsequent technical amendment strengthened the program's commitment to families with children, and established a national goal of 15 percent for units with 3 or more bedrooms. While individual sites are not required to meet this more stringent threshold, they are required to give priority to the selection of projects with three bedroom units.

Exhibit 1.9 describes the sites' performance on these two criteria based on the size distribution of completed units. The proportion of two- or more bedroom units ranges from a minimum of four percent in one site to a maximum of 100 percent in 8 sites, with a median value of 80 percent. Twenty-seven sites have met or exceeded the 70 percent HUD requirement. The proportion of three- or more bedroom units is considerably lower, however, ranging from 0 to 100 percent, with a median value of 20 percent. Nineteen of the 34 sites have met or exceeded the national target of 15 percent.

EXHIBIT 1.9
DISTRIBUTION OF SITES BY UNIT SIZE¹

	<u>Number</u>
Percent of Units With Two or More Bedrooms	
< 70 percent	7
70 - 79	6
80 - 89	10
90 - 99	3
100 percent	8
Median	80 percent
Percent of Units With Three or More Bedrooms	
None	6
1 - 14 percent	9
15 - 30	6
31 - 44	6
45 - 60	4
Over 60	3
Median	20 percent

¹. Data reflect site averages generated from the 8/86 C/MI, and are based on completed units only.

1.4.3 Serving Very Low-Income Families In Substandard Housing

Another important objective of the RRP is to serve very low income families residing in substandard housing. Presumably, this could be accomplished by renovating vacant buildings and making them available for low income occupancy. However, HUD has explicitly proposed a performance measure that is designed to encourage the renovation of occupied properties. The measure reflects the proportion of completed units that are occupied by very low income households who had lived in the project prior to rehab. Thus, both sites that chose to renovate vacant properties and those that experienced high mobility rates would score low on this criterion.

Exhibit 1.10 shows the distribution of the sample sites according to the proportion of very low income tenants served in place. As is evident from the chart, the sample sites display a wide degree of variation on this measure of program performance. In five sites, none of the post-rehab tenants had been previous residents of the projects. In the remaining sites, the proportion of such households served ranged from 6 to 81 percent, with a median value of 32 percent.

Exhibit 1.11 presents information on the proportion of units which were vacant prior to rehab and the proportion of initial occupants who moved before the renovation was complete, stratified by the proportion of low income households served in place.¹ It also shows the

1. As described elsewhere in this report, pre-rehab data are not always reliable. Vacancy rates may in part reflect moves prior to the filing of the pre-rehab C/MI data. In these instances, the C/MI data would overstate initial vacancy rates and understate the extent of mobility, but the estimate of low income households served in place would not be affected.

EXHIBIT 1.10

DISTRIBUTION OF SITES BY
 VERY LOW INCOME HOUSEHOLDS SERVED IN PLACE

<u>Proportion of Units Occupied by Very Low Income Households Who Were Prior Residents</u>	<u>Number of Sites</u>
None	5
1 -25 percent	10
26 - 50 percent	12
Over 50 percent	7
Median	32 percent

1. Data reflect site averages generated from 8/86 C/MI based on completed projects.

EXHIBIT 1.11

MOBILITY RATES, VACANCY RATES, AND POST-REHAB INCOME MIX
 BY PROPORTION OF VERY LOW INCOME HOUSEHOLDS SERVED IN PLACE¹

<u>Proportion of Units Occupied by Very Low Income Households Who Were Prior Residents</u>	<u>Average Mobility Rate</u>	<u>Average Pre-Rehab Vacancy Rates</u>	<u>Total Proportion of Units Occupied by Very Low Income Households</u>
None	0.75	0.82	0.71
1 -25 percent	0.45	0.59	0.69
26 - 50 percent	0.26	0.31	0.70
Over 50 percent	0.14	0.14	0.75
Median	0.25	0.32	0.78

1. Data reflect site averages generated from 8/86 C/MI based on completed projects.

overall proportion of units that were occupied by very low income households after rehab (i.e., including recent in-movers). Much of the sample variation in the proportion of low income households served in place reflects the initial occupancy of RRP projects. Sites with the lowest scores on this measure of program performance tended to renovate vacant buildings. Mobility rates were also significantly higher among the lower scoring sites.¹ Obviously, to serve a high proportion of existing residents, mobility rates must be kept fairly low.

In contrast, a site's performance as measured by the HUD criteria does not reflect its current proportion of very low income tenants (i.e., including new arrivals). The proportion of all post-rehab tenants with incomes below 50 percent of the area-wide median ranged from 20 to 100 percent, with a sample median of 78 percent. The correlation between this statistic and HUD's performance measure is positive, but statistically insignificant. Thus, while the program is clearly serving a high proportion of very low income families, sites differ significantly in the extent to which such families had been previous residents of the projects.

1.4.4 Minimizing the Public Contribution

Another major objective of the RRP is to minimize the amount of public funds that are used to support the renovation. Program regulations set the maximum RRP grant at \$5,000 per unit. However, communities can request exceptions to this ceiling, either on a program-

1. The correlation coefficients between this third performance measure and a site's initial vacancy and mobility rates were -0.78 and -0.64, respectively. Both coefficients were statistically significant at a one percent confidence level.

wide or project-specific basis. Eight of the sample sites were granted at least a limited waiver to the national standard. Sites can also augment the RRP grant with other public funds (for example, loans or grants supported under CDBG). While the RRP grant is limited to 50 percent of the rehab costs up to the \$5,000 maximum, the non-RRP match can come from either public or private sources. As a result, total public expenditures can and do exceed the designated RRP maximum by a significant amount.

The performance of the sample sites according to this fifth criteria of program success is presented in Exhibit 1.11. Following HUD's procedures, the public contribution is defined as the sum of any government-sponsored grants or loans, plus 20 percent of any tax-exempt mortgage bond proceeds.¹ Using this definition, total public expenditures in the sample sites ranged from \$1,259 to \$15,101 per unit, with a median value of \$4,294. Nine sites exceeded \$5,000, 4 sites spent exactly that amount, and 21 sites spent less than the designated maximum. Public expenditures per unit in a given site were highly correlated with its average rehabilitation costs². As a result, this performance measure tends to reward sites that undertook less intensive renovation jobs.

1.4.5 Leveraging Private Funds

Finally, the Rental Rehab program attempts to maximize the leveraging of private monies through its 50 percent matching

1. Chapter 5 establishes an alternative measure that reflects variations in the terms as well as the sources of funds.

2. The correlation coefficient was 0.75, which is significant at a one percent confidence level.

requirement. The sites' performance on this sixth criteria is also presented in Exhibit 1.12. The ratio of public expenditures to the total cost of the rehabilitation ranged from a minimum of 0.26 to a maximum of 0.88, with a median value of 0.48. Half of all sites had ratios between 40 and 50 percent. The sample median of 0.48 implies that about \$1.08 of private funds were raised for every public dollar expended. Obviously, the lower the ratio, the more successful the site has been in leveraging private funds. In the most successful site, one dollar of public expenditures generated \$2.85 of private commitments. In the least successful site, the private contribution dropped to about \$0.14.

1.5 Performance Trade-Offs

The different program objectives describe above may be conflicting under certain circumstances. For example, if the housing market is relatively tight, a site may have to increase the subsidies to private owners in order to produce units that are affordable to low-income households. Thus, the site would have to score low on one factor in order to do well on others. Before one can understand the strengths and weaknesses of the RRP approach, one must first understand the nature and the extent of any such trade-offs, as well as the circumstances under which they occur.

As a start, it is useful to examine the correlation between the various measures of program success in order to judge the extent to which a site's performance on one criteria appears to affect or predict its performance on others. Exhibit 1.13 presents correlation coefficients for the following site-specific variables: (1) the ratio

EXHIBIT 1.12

DISTRIBUTION BY TOTAL PUBLIC COSTS
AND LEVERAGING RATIOS¹

	<u>Number of Sites</u>
Total Public Costs per Unit	
< \$2,000	4
\$1,001 - \$3,000	5
\$3,001 - \$4,000	6
\$4,001 - \$5,000	10
\$5,001 - \$6,000	3
\$6,001 - \$7,000	2
Over \$7,000	4
Median	\$4,294
Total Public Contribution as Percent of Total Rehab Costs	
< 30 percent	3
31 - 40 percent	5
41 - 50 percent	17
51 - 60 percent	3
61 - 70 percent	3
Over 70 percent	4
Median	0.48

1. Data reflect site averages generated from the 8/86 C/MI and refer to completed projects only.

EXHIBIT 1.13
CORRELATION COEFFICIENTS OF THE SIX PERFORMANCE MEASURES

	<u>Factor 2</u>	<u>Factor 3</u>	<u>Factor 4</u>	<u>Factor 5</u>	<u>Factor 6</u>
<u>Factor 1</u> : Ratio of Rents to FMRs	-0.072	-0.031	0.151	-0.029	0.257
<u>Factor 2</u> : Percent of Units with 3 or more Bedrooms		-0.132	0.330*	0.084	-0.139
<u>Factor 3</u> : Percent of Very Low Income Tenants Served In Place			-0.294*	-0.103	0.087
<u>Factor 4</u> : Total Public Expenditures Per Unit				0.570***	-0.080
<u>Factor 5</u> : Ratio of Total Public Expenditures to Rehabilitation Costs					0.162
<u>Factor 6</u> : Proportion of Grant Allocation Expended on Completed Projects					1.000

*** Significant at 0.01 percent
 ** Significant at 0.05 percent
 * Significant at 0.10 percent

of gross rents to FMRs; (2) the proportion of three or more bedroom units; (3) the proportion of tenants with very low incomes who lived in the building prior to rehab; (4) total public contribution per unit; (5) total public contribution as a share of rehab costs; and (6) the percent of grant funds expended on completed projects. Note that only one indicator was used for each criteria of program success in order to simplify the exposition. However, the results are effectively the same if one employs the alternative measures described above.

Perhaps the most striking pattern revealed by the data is the lack of correlation between most of the performance measures. In general, a site's performance on one factor does not predict its performance on others. When sites are ranked according to their relative performance on each criteria, only four sites fall in the lower third of the distribution on more than half of the performance measures (i.e., four or more); no site falls in the upper third of the distribution in more than three performance categories. The typical site scores high in some categories, but average or below average in others.

However, there are a few instances in which the different measures of program success tend to complement or hinder success on the others. Sites with relatively low public expenditures per unit tended to score high on the proportion of very low income tenants served in place (a reinforcing trend). As documented more fully below, this reflects a combination of two factors: the higher cost associated with the rehabilitation of vacant units and the positive relationship between mobility rates and rehab costs in previously occupied projects. Sites

with relatively low public expenditures per unit also achieved relatively high leveraging ratios (another reinforcing trend), but tended to develop fewer three-bedroom units (a trade-off). The relationship between maximum leveraging and minimum public costs was particularly strong.

1.6 Overview of the Report

The foregoing has attempted to highlight national objectives for the RRP (as embodied in HUD performance criteria) and to identify the range of outcomes achieved by the sample sites. The remainder of this report seeks to explain variations in performance and to provide an overall assessment of program operation to date.

Chapter 2 focuses on the ways grantees have designed and implemented their programs. This begins with a description of the administering agencies and the process by which local design decisions were made. Subsequent sections focus on local choices related to subsidy type, neighborhood selection, program outreach and marketing, and program administration. The final section reviews local program objectives and the tradeoffs in implementation faced by the sites.

Chapter 3 focuses on the tenant assistance component of the program, beginning with the role of the PHA in issuing certificates or vouchers to eligible households. Section 2 of the chapter looks at the use of tenant assistance resources generally, and Section 3 focuses on the efforts of the programs to minimize the displacement of existing tenants.

In Chapter 4, tenant issues are examined in more detail, focusing on the characteristics of tenants served by the program and the

affordability of the renovated units. In addition, the chapter examines the extent of mobility and/or displacement under the program and assistance provided to households who move from the Rental Rehab projects.

Chapter 5 focuses on the properties being renovated under the program and, in particular, the motivations of property owners who choose to participate in the Rental Rehab program. The chapter also provides a detailed review of the program from a financial perspective, including the extent to which RRP funds were necessary to stimulate the repair of the properties.

Finally, Chapter 6 looks at the physical conditions of the RRP properties — both before and after rehabilitation — and the types of repairs that have been funded with RRP subsidies. A summary of the study findings is provided in Chapter 7.

CHAPTER 2

PROGRAM DESIGN AND IMPLEMENTATION

As noted in Chapter 1, this study was designed to explain as well as to evaluate. Since the Rental Rehabilitation Program (RRP) allows local agencies so much discretion in program design, a primary task is to explain the choices those agencies have made with respect to basic program design and administrative models. Of major interest here is whether they have in fact chosen widely varying approaches to program implementation or whether one or two models tend to dominate. Once we know what has been done, we can examine possible relationships between implementation techniques and program effectiveness.

The chapter begins with a detailed discussion of the programs' overall administrative structure and the way they approached the process of program design in their localities. Section 2.2 reviews one of the most important design decisions in the RRP -- the choice of a subsidy mechanism. Another key design feature -- neighborhood targeting -- is examined in Section 2.3. Community approaches to outreach and project selection are examined in Section 2.4. Section 2.5 reviews administrative processing techniques, focusing on contrasts between traditional agency approaches and more "streamlined" techniques that assign a larger role to private sector participants. Section 2.6 considers overall relationships between agencies' stated RRP objectives, actual strategies, and performance, highlighting tradeoffs faced in program design and implementation. Finally, Section 2.7 summarizes key findings from earlier sections.

The discussion in Chapter 1 showed that the RRP has several objectives and that some of these objectives may well conflict in practice. Because of this, it is difficult to rate local Rental Rehabilitation programs on a single scale. Doing so might mask important findings, averaging out scores for agencies that are performing exceptionally well by one criterion and exceptionally badly by others. On the other hand, ratings using a large number of criteria can confuse evaluation, making it difficult to identify important patterns.

As a compromise, in this chapter we primarily focus on two important objectives most closely related to administrative issues: the ability to commit funds in a timely manner and success in using public funds to leverage private investment. As shown in Chapter 1, the sample sites showed wide variation on both of these measures. Nevertheless, the restriction of the sample to sites which had completed at least one project means that all of the sample sites are relatively good performers with respect to initial program production. The reader is also advised that outcome data presented in this chapter are typically weighted to reflect the administration of the average grant dollar. The use of weights is noted in the chapter exhibits; a detailed description of sample selection and weighting procedures is provided in Appendix A.

2.1 Administrative Structure, Prior Experience and the Local Program Design Process

This section begins by describing the types of agencies selected to administer the RRP in our sample communities and reviews their prior experience in operating rehabilitation programs. It then

discusses how they went about designing their own adaptations of the program, focusing on the degree to which other public and private agencies were involved in the process.

2.1.1 Administrative Structure

The HUD RRP design implies that the typical administrative arrangement will be one in which the rehabilitation itself is administered by a local housing rehabilitation agency and a separate public housing authority (PHA) administers tenant assistance component of the program (Section 8 certificates and vouchers). Exhibit 2.1 shows that this was the dominant, but not the only, arrangement among our sample communities. While 25 sites conformed to this model, in 6 sites the program was administered under an arrangement in which the rehabilitation unit and the PHA were separate departments in the same umbrella agency, and in three sites a PHA administered both components of the program.

The Typical Model

Among the 25 rehabilitation entities under the typical model, 17 were city community development (CD) agencies (agencies that are responsible for the local CDBG program), and 4 were county CD agencies. Other local government agencies played the lead role in two sites: an independent Redevelopment Authority in Greensboro, and a City Housing Department in Chicago. In two other sites, the lead role was played by private nonprofit corporations acting under contract to the city: the Philadelphia Housing Development Corporation (an institution with a substantial track record in running housing programs for the city), and Urban Development Resources, Inc., of Newark.

EXHIBIT 2.1

DISTRIBUTION OF SITES BY TYPE OF AGENCY,
PROGRAM SIZE, AND PRIOR EXPERIENCE

	<u>Number of Sites</u>
TYPE OF AGENCY	
RRP Agency with Separate PHA	
City CD Agency	14
City CD Agency/Decentralized	3
Other City Agency	2
City Private Non-Profit	2
County CD Agency	<u>4</u>
Subtotal	25
RRP and PHA Separate But in Same Agency	
City CD Agency	2
Other City Agency	2
County CD Agency	<u>2</u>
Subtotal	6
PHA Operates RRP	3
RRP Demonstration Experience ¹	
Some	15
None	19
Other Rehab Experience ²	
Above Average	13
Average	12
Below Average	9

1. Includes sites with one or more completed demo units as of summer 1986.

2. Based on HUD field office experience ratings as confirmed by reported unit production.

Only three of these agencies delegated any major RRP administrative functions to outside organizations. The Department of Planning and Community Development which is responsible for the RRP in Houston, delegated most of its technical functions to the city's public works department. San Francisco's Mayor's Office of Housing and Economic Development coordinated program activities but also delegated some functions to private neighborhood Housing Development Corporations operating in the RRP neighborhoods. Los Angeles' Community Development Department ran a large part of the program itself but also allocated a sizeable share of its grant funds to be independently administered by the city's Community Redevelopment Agency. In addition, some processing functions were delegated to 21 field offices operating in target neighborhoods across the city.

Other Administrative Arrangements

Of the six umbrella agencies that contained both RRP and PHA subunits, four were CDBG agencies (two city and two county). The two non-CDBG agencies were Milwaukee's Department of City Development and San Diego's Housing Commission. Two of the three PHAs that ran both aspects of the program received their assignments because they were the entity traditionally responsible for implementing CD housing programs. San Antonio contracted out the job of implementing the RRP to the local PHA because it had stronger experience with rehabilitation programs.

2.1.2 Prior Experience of Administering Agencies

All of the agencies in our sample had some prior experience in administering rehabilitation programs, but the extent of that experience varied widely. Several had implemented large scale CDBG programs. For

example, reported 1981-86 CDBG rehab program output totaled over 5,000 units in 3 sites and over 1,000 units in 6 others. On the other hand, some agencies were relatively new at the game and had only a few completions under their belts. Among all sample communities, 15 had participated in the Rental Rehabilitation Demonstration (completing at least one project by mid-1986).

2.1.3 Influence on Performance Outcomes

Does a community's RRP administrative structure or its prior rehab experience have a substantial impact on program outcomes? Exhibit 2.2 offers preliminary evidence suggesting mixed results. In the exhibit, we have grouped local programs into four categories based on their performance with respect to production and leveraging. A site is rated as high or low depending on whether it scored above or below the median for the performance measure at hand i.e., sites in the "High Production-High Leveraging" group were above the median with respect to both measures.

Administrative Structure

One might expect that the degree of administrative centralization would influence performance. Control should be highest where one agency (in this case a PHA) administers all program functions. An umbrella agency containing both an RRP unit and a PHA would come next by this measure, followed by the "typical model" (RRP agency with an institutionally separate PHA). Finally, those agencies that delegated functions to outside groups might be expected to have the most difficult control problems, although they might gain through broader community involvement in program operations.

EXHIBIT 2.2

**INFLUENCE OF ADMINISTRATIVE STRUCTURE AND
EXPERIENCE ON PERFORMANCE
(Percent of Sites)**

	High Production High <u>Leverage</u>	High Production Low <u>Leverage</u>	Low Production High <u>Leverage</u>	Low Production Low <u>Leverage</u>	<u>Total</u>	<u>N</u>
All Sites	21%	29%	29%	21%	100%	34
Administrative Structure						
PHA operates program	33%	-	66%	-	100%	3
Umbrella agency with RRP/PHA	-	33%	50%	17%	100%	6
RRP with separate PHA						
No delegation of functions	27%	27%	23%	23%	100%	22
Delegation of functions	-	66%	-	33%	100%	3
HUD Staff Experience Rating						
High	15%	46%	31%	8%	100%	13
Average	17%	17%	42%	25%	100%	12
Low	33%	22%	11%	11%	100%	9
Participation in RRP Demonstration						
Participants	11%	27%	33%	28%	100%	15
Nonparticipants	31%	31%	25%	13%	100%	19

The data do not lend much support to these hypotheses. None of these administrative types clusters dominantly in any single performance category. For example, we find that the agencies under the typical model (without delegation) have a slightly higher percentage in the "high production-high leverage" category (27%) than the average for all sites (21%), but they are also significantly represented in the other three performance categories as well. The umbrella agencies are somewhat over represented in the two middle performance categories (high production-low leverage and its opposite). The number of sites in the other two administrative types is too small (3 each) to support strong conclusions, but in neither case did all sites fall at the same position on the scale.

It appears that administrative structure in and of itself is not a strong determinant of performance. Given acceptable market conditions and sufficient staff skill and diligence, it seems likely that the RRP could be made to work effectively under any of these structural alternatives.

Prior Rehab Experience

The influence of prior rental rehab experience on RRP performance is similarly less strong than might have been expected. Sites with high experience are underrepresented in the lowest performance category (8% compared to 21% for the sample as a whole), but are also underrepresented in the highest performance category (15% compared to 21%). They are most strongly clustered in the high production-low leverage group, suggesting (tentatively at least) that

experienced agencies are willing to liberalize terms as needed to secure owner interest and participation.

Perhaps the most interesting finding here is that the low-experience sites are the most strongly concentrated in the high performance category (33% compared to 21% for the sample as a whole) even though they are significantly represented in all other performance categories as well. This suggests that while the RRP differs in many respects from past public rehab programs, those differences are not so complex that they cannot be mastered effectively by relatively inexperienced agencies. Again supporting the conclusion that the relationship between RRP performance and prior experience is not straightforward, it is the "average experience" group that is most overrepresented in the lowest performance category (25% compared to 21%).

Participation in the Demonstration

Although the relationships are not strikingly different, it appears that the sample sites that participated in the demonstration were at least somewhat less successful at operating the program than those that did not.¹ Among the participants, 11% were in the highest performance category (compared to 31% for the nonparticipants) and 28% were in the lowest performance group (compared to 13% for the nonparticipants). This observation does not suggest that experience in

1. Participation here is defined as entailing the completion of at least one unit under the demo prior to the time of the site visits. When sites are grouped into three categories (high, medium, low) based on actual output under the demonstration, mean leveraging ratios are virtually identical. Sample sites with no demonstration experience showed the lowest commitment rates and sites with low experience showed the highest.

the demonstration did not prepare agencies for more effective RRP operation. Variations such as those shown here may be explained by differences in local market conditions that affected both programs.

2.1.4 The Local RRP Design Process

While the basic features of RRP design are established in HUD regulations, localities still have to make a number of design decisions as to how their programs are to be implemented; e.g., choice of subsidy mechanism, approach to neighborhood targeting, and determination as to the types of projects that will be approved for the program. In 91% of our sample communities, those design decisions were made by the agencies selected to administer the program. The three sites where this was not the case were Houston (design by the Planning Department and later given to the CD agency to administer), Newark (design by the Mayor's Office with implementation later delegated to a nonprofit corporation), and San Antonio (design by CD staff, with implementation contracted out to the PHA).

Based on information provided by city respondents, PHAs were in most cases involved in the design process, although their role was relatively passive. PHAs were described as "actively involved" in the design of the program in 26 percent of the sites (excluding the 3 communities in which the PHA ran the program); PHAs were described as having been consulted in just over half of the remaining sites. Otherwise, there was comparatively little outside involvement in program design decisions. Mayors and other city officials were consulted in 41% of the sites, but were actively involved in only one case. Citizen groups were consulted by 44% and private lenders by 26%, but in no case

were either actively involved. HUD staff were consulted about design decisions by 53% of the sites, and HUD technical assistance contractors by 21%. The following sections describe the specific implementation approaches arrived at by this process.

2.2 Selection of the Subsidy Mechanism

One of the key design choices faced by local rental rehab programs is the method by which RRP subsidies will be delivered. Options range from up front capital subsidies with no requirement for repayment (grants and "forgivable" loans) to direct city loans with payments beginning immediately or deferred until some future date. Interest subsidies, whereby city funds are used to write down the interest rate on loans offered by private lenders, may also be employed.

Each of these approaches has advantages in some situations. Non-repayable forms offer simplicity in administration and may be highly attractive to potential program participants. Low interest loans, on the other hand, may be sufficiently attractive in some markets to stimulate investor demand, while also generating a payback of funds that can be used to initiate additional projects in the future. Finally, under the interest subsidy approach, program funds may be used to leverage private loans covering the full cost of rehab.

In addition to the selection of the RRP delivery mechanism itself, grantees must determine the amount of subsidy that will be provided to each project (subject to the per unit dollar limits set by the program) and whether to provide additional public funds to deepen the subsidy in selected cases. The choices the sites have made, the

rationales behind them, and the impact on overall program performance are the subjects of this section.

2.2.1 Subsidy Types

Exhibit 2.3 shows the types of subsidies offered by the 34 sites visited for this study. As shown in the exhibit, RRP delivery mechanisms include grants, deferred payment loans (both forgiven and repayable), direct (self amortizing) loans, and interest subsidies. Allowing for the use of more than one approach in each site, forgivable DPLs were the most commonly offered delivery mechanism (15 sites), followed by repayable DPLs (12 sites) and direct loans (10 sites). Outright grants and interest subsidies were the least common forms, offered in 5 and 2 communities, respectively.

While the vast majority of rental rehab programs selected a single subsidy mechanism, seven of our sample sites offered two or more different subsidies. Sites offering multiple subsidy types were primarily larger cities and counties (population over 1 million) but also included two sites in the smallest size category. Typically, the use of multiple subsidies involved adding some provision for deferral to a program in which the basic mechanism was a fully amortized direct loan. In three cases, however, repayable and non-repayable forms were mixed.

Non Repayable Subsidies

Taken together, grants and forgivable deferred payment loans were the most common mechanisms used delivering RRP subsidies. Grants were the sole RRP mechanism in three sites, and forgivable DPLs were

EXHIBIT 2.3

SUBSIDY TYPES OFFERED IN RRP PROGRAMS ¹

<u>Type</u>	<u>Number of Sites</u>	<u>% of Sites</u>
Grant	5	15%
Forgivable DPL	15	44%
Repayable DPL	12	35%
Direct Loan	10	29%
Interest Subsidy	2	6%

1. Sites offering more than one subsidy appear more than once.

PROGRAM APPROACHES FOR DELIVERING RRP SUBSIDIES

<u>Type</u>	<u>Number of Sites</u>	<u>% of Grant Dollars</u> ¹
Single Delivery Mechanism:		
Grant	3	8%
Forgivable DPL	14	37%
Repayable DPL	7	19%
Direct Loan	3	8%
More than One Mechanism:		
Direct Loan and Repayable DPL	4	16%
Mixed (forgivable and non-forgivable forms)	<u>3</u>	<u>12%</u>
	34	100%

1. Weighted to reflect the administration of the average grant dollar.

used as the sole delivery mechanism in 14 sites. Thus, 17 sites representing about 45% of all RRP grant dollars provided the subsidy in a wholly non-repayable form.

Whether the subsidy was labeled a grant or a loan appears to have depended largely on perceptions about the marketability of the two forms, along with, in a few cases, previous experience with one or the other approach. Despite the fact that grants and forgivable DPLs are equivalent in terms of the subsidy provided, grants presumably sound more appealing to owners and lend themselves to extremely straight forward marketing. However, internal marketing and/or city politics, also seems to have played a role in this choice, with respondents in several of the sites offering forgivable loans indicating that this form was deemed more desirable because it avoided the appearance of a "giveaway."

A second factor affecting this choice relates to the relative control the mechanisms provide over owners. Specifically, the DPL offers a convenient approach for enforcing compliance with program objectives by providing for annual forgiveness of some portion of the principal amount based on compliance with key program requirements (e.g., prohibitions on condo conversion or discrimination against assisted tenants.) With a few exceptions, DPLs offered by the sample sites provided for assumable 10 year loans, with principal forgiven at a rate of 10% per year. While most sites offered the loan at zero percent interest, about a third attached a rate to the note (ranging up to 14%) payable if the conditions were breached. Almost three quarters of the DPL sites indicated that "control over project owners" was important or

very important in subsidy selection, compared to none of the grant sites. Nevertheless, the grants used under the program were similarly "conditioned" and often provided for a forgiveness schedule similar to those used with DPLs. In the one site where the originally selected grant mechanism failed to include proper conditions, the mechanism was changed (at the request of HUD field office staff) to a forgivable DPL.

Repayable Subsidies

Despite the fact that HUD's TA materials have strongly promoted the use of non repayable subsidies (these being regarded as the most simple and attractive subsidy types), 14 of the sample sites, representing about 43% of all grant dollars, opted for repayable loans as the RRP delivery mechanism. In six of these sites the dominant subsidy was an immediately repayable direct loan, and in eight the dominant approach was a deferred payment loan.

The direct loan sites include three that provide direct loans only, and three additional sites that rely principally on direct loans but also offer deferred payment schedules in some cases¹. Terms for direct loans ranged from a low of 5 years, up to 20 years in one site where the length of the loan was varied depending on the economics of each project. Ten year terms were, however, most common. Interest rates on direct loans were between zero and 3 percent in all cases except one where direct loans were offered at 5%.

1. In these sites, deferral is automatically available to owners who obtain conventional financing for the non-RRP share of the rehab costs. At the time of data collection, however, few completed projects involved this subsidy type. In one of these sites, program staff suggested that the owners avoid the DPL because they don't want to be locked into a longer term.

For the eight sites that principally relied on repayable deferred payment loans, rates and terms varied considerably. Three of the sites set a fixed term at which time a single balloon payment was due, and three others geared balloon payments to the end of the private rehab loan or first mortgage (up to 40 years in one case). One site provided for amortized payments following a 3 to 5 year deferral period, and one required repayment only upon sale of the property. Interest rates for deferred loans were most commonly zero (4 sites), but exceeded 5% in three others.

Among sites that selected a repayable mechanism—deferred or not—political constraints as well as program objectives appeared to play an important role in this decision. A large proportion (57%) of the sites with repayable loans indicated that a political need to obtain a payback of funds acted as a constraint in subsidy selection. Alternatively, a few sites indicated a more positive desire to generate funds for additional future projects.

Overall, however, the most frequently cited reasons for selecting a particular subsidy approach (forgivable or repayable) were attractiveness to owners (cited as very important in 73% of all sites) and administrative simplicity (cited as very important in 41%). The subjective nature of these factors is demonstrated by the fact that different subsidy approaches claim these with much the same frequency. Thus, sites choosing repayable versus forgivable types are just as likely to see their subsidy as attractive to owners. Similarly, the desire for administrative simplicity may have very different implications in different sites. While a substantial number of sites

selected a grant or forgivable DPL because they perceived it as administratively efficient, the same is true for sites with repayable loans. As an example, one site which provides a 3% direct loan, specifically selected this approach because it was consistent with loans already being provided under a CDBG-funded rehab program and therefore familiar and simple to administer.

Mixed Subsidies

Three of the sample sites (representing 12% of all grant dollars) provided both repayable and non repayable subsidies. In one, the program provided both direct loans and grants; however, grants were available only to low-income owner occupants—a group whose participation the program sought to encourage. Similarly, in the second site, the program offered primarily repayable subsidy types (including interest subsidies and several different direct loan arrangements), however, exceptions were made in the case of seismically deficient units, which were deemed more costly to repair and, again, were targeted by the program. Finally, in the third site the program provided interest subsidies and direct loans, along with forgivable DPLs. The DPLs were offered on a case by case basis with the subsidy amount to be established through gap analysis. An explicit goal of this program was to provide a choice of subsidies that would appeal to a range of owners and meet a variety of property needs.

2.2.2 Other Objectives in Subsidy Selection

As indicated above, attractiveness to owners and administrative simplicity, figured most highly in subsidy selection decisions, reported as very important factors in 73% and 41% of the sites. Maximizing unit output and leveraging were next in importance, identified as very important factors in 35% and 26% of the sites respectively, and associated most strongly with repayable subsidy types. Finally, local politics appeared to have operated as a constraint in subsidy selection for over half of the sites which provided repayable subsidies, affecting nearly a quarter of the sample sites overall.

Beyond this, however, in a few cases the subsidy mechanism itself was used to promote other distinct program objectives. As noted above, one of the mixed subsidy programs provided grants (in lieu of direct loans) to a target group of lower-income owner-occupants. Similarly, within the direct loan portion of this program, interest rates charged varied depending on owner income and use of minority contractors. Two other sites offered more favorable terms to some properties, based on ownership type (non-profit vs. for profit) and minority contractor participation in one, and unit size (favoring 2 and 3 bedroom units) and target area in another. At the time of the site visit, another site was in the process of adding a non-repayable subsidy specifically to encourage the rehabilitation of larger units.

2.2.3 Changes in Subsidy Approach

The RRP design is intended to offer sites maximum flexibility in gearing programs to local needs and adjusting them to meet changing circumstances. Between the program's inception and the summer of 1986,

10 sites took advantage of this flexibility to substantively alter their subsidy mechanisms. However, these initial changes were overwhelming in the direction of liberalizing or simplifying the terms of the subsidy. Altogether, seven sites liberalized terms: four switched from a repayable subsidy to a grant or forgivable DPL; two slashed interest rates on direct loans; and one switched from a direct loan to a deferred loan. In each of these cases, the switch was designed to boost lagging production and represented a trade off between this measure of program performance and the extent of payback achieved by the program. In almost all cases the changes occurred relatively early on (within the first year of operation) as a direct response to low application rates. In two of these programs, however, the change was not effected until spring of 1986--shortly before the data collection for this study.

Trade-offs between production and leveraging were evident in two additional sites--one in which CDBG funds were made available to supplant a portion of the owner's contribution and another in which a gap financing approach was dropped in favor of a straight 50% of cost calculation.

Finally, only one site ran counter to the trend, moving quite recently from a grant to a repayable DPL. This change was intended to create a source of renewable funds, a step considered desirable in light of cut backs in CDBG funding. Not surprisingly, however, concerns were expressed -- both among program and HUD field office staff -- about the potential negative impacts of this change on program production.

2.2.4 Subsidy Amounts and Cost Limits

While the type of subsidy offered by a site may play a key role in the marketability of the program, the level of subsidy is also a design choice open to rental rehab grantees. Program regulations provide that RRP subsidies may be provided for up to half of the total rehab cost subject to a dollar cap of \$5000 per unit, except in high cost areas where a higher amount may be approved. Sites are, however, free to set lower limits if desired or to attempt to minimize the subsidy amount on a case by case basis through the use of gap financing analysis.

Overall, the vast majority of sites worked within the \$5,000 subsidy cap. Five sites (accounting for 22% of all grant dollars) had requested and received high cost exemptions from HUD with the highest cap at \$8,750 per unit. A few additional sites had requested and received exceptions for one or two projects. Only one site imposed a subsidy cap that was lower than \$5,000; this was a county program which limited the subsidy to a \$2,000 grant.

In establishing the amount of subsidy to be provided to individual projects, there was again little deviation from HUD's program guidelines, and little attempt use gap financing techniques. Overall, 32 of the 34 sites provided the subsidy as a fixed proportion of rehab costs. This proportion was 50% in all sites save one, where RRP funds were provided for 33% of project costs in an explicit attempt to avoid oversubsidization.

Only two of the sample sites used gap analysis to determine the amount of the subsidy to be provided. In one site, the program had established rigid limits on allowable development and operating costs, as well as owners' rates of return. Subsidy amounts (delivered as a zero percent, repayable DPL) are calculated individually, with payment due in 10 years or at the end of the first mortgage. In the second community, gap analysis is used to calculate the subsidy amount under one of three subsidy mechanisms available. As noted above, one other site began the program using the gap technique, but subsequently dropped it in favor of the simpler 50% of cost approach.

Overall, then, gap financing in the strictest sense is exceedingly rare in the rental rehab program--limited in use to two of the 34 sample sites, and in one of these communities, to one of three available subsidy approaches. However, three additional sites implemented a variant of gap financing by adjusting interest rates and/or loan terms to accommodate the needs of individual projects. Except in the site offering multiple subsidies, the use of gap financing, as broadly defined, was limited to direct loans or repayable DPLs.

2.2.5 Use of Other Funds

Rental Rehab subsidies are limited to half of the total rehab costs, thus providing for at least a one to one leveraging ratio with other sources of funds. Leveraging of private funds, however, may be substantially less, depending on whether the community elects to provide additional public funding to rental rehab projects. Overall, we found the use of other public funds (primarily CDBG) to be substantial, with

21 of the 34 sample sites (62%) making other public funds available for use in Rental Rehab projects.

Typically, the use of public funds was decided on a case-by-case basis, depending on the financial needs of a particular project. However, in 2 of the 21 sites providing additional public funding, a standardized package combining RRP funds and CDBG funds was employed. In one site, combined funds were provided as a direct loan for 90% of cost. In the other, one of the options available to owners combined CDBG loans with rental rehab loans to cover 100% of project costs.

Not surprisingly, availability of additional public funds tended to be more common when the RRP subsidy mechanism provided for repayment. Ten of 14 sites (71%) providing repayable loans offered additional subsidy, compared to eight of 17 (47%) sites with grant or grant like mechanisms. All three of the mixed subsidy sites provided additional funding for at least some projects. Finally, the five sites that attempted to vary the terms of the RRP subsidy with the individual project's needs all used additional public monies.

2.2.6 Variations in Subsidy Approaches

As discussed previously, selecting a subsidy mechanism that was attractive to owners was a paramount concern in the choice of RRP delivery mechanisms.¹ However, what is attractive in one market may be less so in another. Exhibit 2.4 shows a breakdown of subsidy types by

1. Only 2 sites related this factor as not important, both of these indicating that a political need to obtain a payback drove the subsidy selection process.

EXHIBIT 2.4

SUBSIDY APPROACH BY SIZE, EXPERIENCE, AND MARKET TYPE
(percentage of sites¹)

	Type of RRP Subsidy				Percentage of sites Offering Add'l Public Subsidy	N
	Grant or Forgiven DPL	Direct Loan	Repayable DPL	Mixed		
<u>City Size</u>						
Under 250,000	55%	27%	18%	0%	27%	11
250,000 - 500,000	50%	10%	30%	10%	70%	10
500,000 - 1 million	67%	17%	17%	0%	67%	6
Over 1 million	19%	9%	39%	33%	100%	7
<u>Experience</u>						
High	48%	14%	14%	24%	86%	13
Medium	28%	14%	51%	07%	65%	12
Low	67%	33%	10%	0%	33%	9
<u>Market Type</u>						
High Rent/High Vacancy	54%	11%	25%	11%	68%	9
Low Rent/High Vacancy (loose)	47%	16%	38%	0%	53%	11
High Rent/Low Vacancy (tight)	32%	16%	24%	28%	84%	11
Low Rent/Low Vacancy	66%	33%	0%	0%	33%	3

1. Weighted to reflect the administration of the average grant dollar.

other factors that might influence this decision, including rehabilitation experience, city size and market type.

Selection of a forgivable versus a non-forgivable form does not seem to be strongly related to the experience or the size of the site. The two smallest size groups selected forgivable and non-forgivable types with roughly equal frequency. Sites in the next largest size group (500,000 to one million) tended to favor non-repayable forms, while sites in the largest group typically opted for repayable or mixed forms. With respect to experience, highly experienced sites again selected forgivable and non-forgivable types in roughly equal numbers. Moderately experienced sites were more likely to select loans, and less experienced sites tended to favor grants or forgivable DPLs.

The breakdown by market type also fails to show any strong relationship. In high vacancy markets, grants and loans were used in roughly equal numbers. In tight markets (i.e., areas with high rents and relatively low vacancy rates), there was some tendency to favor the loan approach, while in 2 of the 3 low rent/low vacancy markets, forgivable subsidies were used. While not shown in the chart, the use of gap financing, as broadly defined, did not appear to be concentrated in any particular type of market, nor was it related to the size or experience of the site.

By contrast, supplementation of RRP funds with other public subsidies appears to follow a definite pattern, with the use of other public subsidies increasing with both city size and experience. All of the sites in the largest population category provided additional public funding, as did 86 percent of the sites with the highest experience

ratings. Sites in high rent areas, especially "tight markets" where vacancy rates were relatively low, were also more likely to supplement RRP dollars with other public funds.

2.2.7 Impact of Subsidy Approaches on Program Outcomes

Exhibit 2.5 presents information on program outcomes by the type of subsidy employed. In addition to presenting one-way breakdowns by subsidy mechanism and the use of other public monies, we present breakdowns for a combined subsidy measure that distinguishes forgivable and non-forgivable subsidies with and without additional public monies. We also present information on variations in program outcomes by market type.

In general, sites offering non-repayable subsidies had the highest commitment rates, although the use of grants was also associated with relatively low leveraging ratios and rather high public costs per unit. Somewhat surprisingly, the use of other public monies was associated with lower commitment rates. Since there was no indication that the offer of additional public funds per se led to slower commitments, this result is more likely related to interactions between the form in which the basic subsidy is provided and market conditions which encourage or discourage rehab investment.

These patterns are illucidated somewhat if one classifies the subsidy mechanism by both type of subsidy and the provision of other public monies. Differences between repayable and forgivable subsidies are extremely small if only RRP funds are employed. However, the differences are quite pronounced for sites which offer additional public assistance. The lowest commitment rates were observed in sites that

EXHIBIT 2.5

PERFORMANCE BY SUBSIDY APPROACH AND MARKET ¹

	Committed Dollars as a Percentage of Total Allocation	Public Funds as a Percentage of Total Cost	Ratio of Rents to FMRs	Total Public Costs per Unit	N
Subsidy Type					
Grants	69%	58%	.81	\$6,742	3
Forgivable DPL	70%	46%	.88	4,870	14
Repayable DPL	45%	52%	.90	4,992	8
Direct Loan	58%	57%	.83	4,734	6
Mixed	51%	56%	.80	4,194	3
Use of Other Public Funds					
Used	54%	55%	.86	\$5,675	21
Not used	68%	44%	.86	3,571	13
No Other Public Funds Provided					
Non-Repayable	69%	44%	.84	\$3,748	9
Repayable	66%	44%	.89	3,172	4
Other Public Funds Used					
Non-repayable	71%	53%	.89	\$6,834	8
Repayable ²	46%	57%	.85	5,120	13
Market Type					
High Vacancy, High Rent	57%	42%	.86	\$4,223	9
High Vacancy, Low Rent (loose)	52%	52%	.85	\$4,734	11
Low Vacancy, High Rent (tight)	68%	60%	.88	\$6,159	11
Low Vacancy, Low Rents	62%	42%	.81	3,093	3

1. Weighted to reflect the administration of the average grant dollar.
2. Includes three mixed sites.

provided supplemental public funding but offered the RRP subsidy as a loan. The highest commitment rates were observed among sites offering forgivable subsidies with supplemental public funds. However, their commitment rates are only marginally above those achieved in sites offering a non-repayable subsidy with no additional public funding, and the latter score considerably higher in terms of leveraging and public costs.

Variations by market type are less pronounced, although some definite patterns emerge. In general, markets with relatively low vacancy rates have higher commitment rates than sites where vacancy rates are high. Controlling for vacancy rates, commitment rates also appear to be higher in areas where rents are relatively high. Thus, the highest commitment rates are observed in low vacancy, high rent areas (i.e., "tight" markets), while the lowest rates occur in high vacancy, low rent areas (i.e., "loose" markets). Patterns with respect to leveraging and the level of public costs appear to be mixed.

The combined effects of subsidy mechanisms and market type are depicted in Exhibit 2.6. The data reveal the strong influence of subsidy type on production rates, but also indicate that market type can act as an important constraint on production, regardless of the generosity of the subsidy offered. Specifically, we see that in all markets forgivable subsidies are associated with higher commitment rates. In tight markets (which show the highest commitment rates overall) use of a forgivable subsidy is associated with higher commitments by one-half, though this may also be due to the willingness

EXHIBIT 2.6
PERFORMANCE BY SUBSIDY AND MARKET^{1,2}

	Forgivable RRP Subsidy			Repayable RRP Subsidy		
	Committed Dollars as Percentage of Total <u>Allocation</u>	Public Cost as a Percentage of Total <u>Rehab Cost</u>	<u>N</u>	Committed Dollars as Percentage of Total <u>Allocation</u>	Public Cost as a Percentage of Total <u>Rehab Cost</u>	<u>N</u>
High rent/Low vacancy (tight)	90%	67%	4	60%	55%	5
High rent/High vacancy	76%	37%	5	30%	46%	3
Low rent/Low vacancy	44%	38%	2	*	*	1
Low rent/High vacancy (loose)	60%	47%	6	44%	52%	5

* Sample size is too small to permit comparisons.

-
1. Weighted to reflect the administration of the average grant dollar
 2. Excludes three mixed sites.

of these sites to use additional funds to cover a greater proportion of total rehab costs. In high rent/high vacancy markets, however, commitments rates are halved when repayment is required despite a tendency to cover a higher proportion of rehab costs. The same is true in loose markets, although it appears that sites in this market are only able to attain modest production levels even when subsidies are offered in a completely non-repayable form. Thus, loose markets provide the most difficult setting for the operation of a rental rehab program, and, as will be shown in Chapter 5, tend to attract investors with a distinct set of motivations and interests.

2.2.8 Lender Participation

Since the RRP is intended to leverage private funds for rehabilitation, it is appropriate at this point to examine briefly the role of grantees in securing lender participation in the program. Although 46% of all completed units involved a private loan, lenders played little "official" role in the program. In general, lenders had little involvement in the design of local programs and only occasionally had the local administering authority made an attempt to enlist lenders in the program.

Overall, in 20 of the 34 samples sites (59%), there was no attempt to solicit lender comments on program design, market the program with lenders, or establish formal or informal arrangements to provide loans under the program. In fact, a large number of sites indicated that obtaining private loan funds was the responsibility of the owner

and that the program's minimal role in this activity was an element of streamlining.

In the 14 sites where there was some official attempt to involve lending institutions, the nature of this involvement varied.

- o In two sites, the programs used existing arrangements with a single local bank to provide below market loans to program participants. RRP funds were used to write down interest rates to 10% in one of the programs and 5% under the other. These were the only examples of the interest subsidy mechanism found in the 34 sites.
- o Four other sites had established a formal arrangement with a local lender. In two cases, the agency used existing arrangements with a lender who had agreed to provide market rate (in one case slightly below market) loans to owners making applications via city programs. In two other sites, the arrangement was specific to the RRP. Three of these four sites indicated that the bank agreement had an important impact on production. One, however, indicated that the lending arrangement was used infrequently and therefore not a factor in the program's progress.
- o Two sites drew on informal relationships with local lenders. One works informally with a lender, which also participates in other city programs, and refers owners who request financing assistance to this source. The other draws rather heavily on its relationship with a community investment corporation (funded by a consortium of banks) which is the usual source of private financing under the program and also provides technical assistance to owners.

Six additional sites contacted lenders concerning the RRP but did not achieve any sort of agreement. In two, the contacts were more in the nature of marketing, and no commitment was sought. In two others, where the programs did seek a commitment, they found lenders supportive but reluctant to establish a formal arrangement in advance. However, in two other sites, program staff indicated that lenders were

unsupportive when approached and that lack of lender participation was an obstacle to progress.

When asked to rate private lenders' response to the program, local officials in 17 sites (50%) indicated that private lenders were either very supportive or supportive of the program. In 8 sites (24%), respondents described lender responses as unfavorable or indicated that lenders were "not interested" in the program, and in 9 (26%) sites program staff indicated no basis for evaluating lender attitudes. Given that very few sites attempted to officially involve lenders, the level of lender participation in a given site tended to relate to general market conditions and the desire and/or ability of individual owners to draw on their existing relationships with lenders to secure rehabilitation financing. For example, program officials in loose markets often pointed to widespread difficulty in securing private loans as a problem. In numerous other sites, however, the small size of the rehab jobs led owners to use cash or to draw on lines of credit rather than secure secondary financing for the RRP.

2.3 Neighborhood Targeting

The second major design decision faced by Rental Rehab programs is the selection of target areas in which to focus program operations. Targeting decisions may be related to the types of properties or owners the program seeks to attract and, in theory, may inform other program decisions such as the nature and depth of the subsidy to be provided. We begin with a general discussion of the neighborhood selection process as it operated in the 34 sites, and then describe the types of areas where rental rehab projects are actually located.

2.3.1 Selection Process

Program regulations for the RRP suggest that the selection of appropriate Rental Rehab neighborhoods is a key to program success. Since rents in Rental Rehab projects are to be determined by market forces, projects must be located in lower income areas and in areas where rents are affordable and likely to remain so. Gentrifying neighborhoods would not be appropriate for the RRP, nor would severely deteriorated neighborhoods since it would be difficult to leverage private investment in such areas. Program regulations define a neighborhood as an area determined by the grantee that surrounds a project and tends to determine, along with the condition of the project itself, the rents that are charged for the units.

To begin, it is important to note that very few of the sample Rental Rehab sites targeted their programs to specific "neighborhoods," in the sense that one or more small areas were selected for intensive or concentrated improvement. Given the relatively small size of the program, the RRP is typically not perceived as a neighborhood improvement program, but rather as a tool for upgrading marginal properties. Thus, grantees tended to be fairly inclusive in establishing eligible areas for the RRP. Moreover, as the program progressed, a number of sites opted to broaden their target areas in an attempt to generate additional demand for the program.

At the time of our visits, 21 sites had adopted an essentially non-targeted approach to the program, accepting projects from any area of the jurisdiction that met HUD's basic eligibility criteria. The

geographic unit used to establish eligible areas was most commonly the census tract, but also included cities or towns (in urban counties), zip codes, and, in a few cases, census blocks.¹ In many cases, areas identified by this process substantially coincided with existing community development areas or clustered into one or more relatively well-defined areas. However, the process occasionally led to "checkerboard" maps or simple listings of tracts against which incoming applications could be matched. In five of the sites, target areas were not designated in advance; instead, projects were qualified individually as applications were received, using either block or building level data.

By contrast, 13 sites opted to select a subset of technically eligible areas, thus imposing local targeting constraints beyond those established by the national program. In 7 sites, the selected areas were identical to existing CD neighborhoods. In the remaining 6, the target areas were selected specifically for the Rental Rehab program.

Several factors appeared to play a role in the selection of a non-restrictive targeting approach on the part of most sites. As noted above, the program is generally not viewed as a neighborhood improvement program, and most sites had no inclination to concentrate RRP activity in a small area. Politics also appeared to have played some role in cities with strong neighborhood organizations, making it difficult to target the program to certain neighborhoods while excluding others.

1. Eligible areas are defined by HUD as those where median income does not exceed 80% of the SMSA median and rents are "generally affordable" to lower income families, meaning that gross rents are at or below the FMR.

However, the major factor appears to have been a perceived need to cast a wide net in recruiting project owners. Sites offering a rationale for non-restrictive targeting typically indicated a need to draw on a larger body of owners to meet program production goals.

Moreover, as the program progressed, pressure to broaden the owner base increased. A total of eight sites within the 34 site sample were forced to relax their original targeting criteria as the program got underway in order to increase or maintain production levels. Two of these moved to a project-based qualification system; three expanded their areas to "all eligible tracts;" and three maintained a targeted subset of otherwise eligible areas, but expanded this set to include additional neighborhoods or to eliminate restrictions on the location of properties containing larger units. Only one site actually reduced the size of its target area, and this action was to eliminate a gentrifying neighborhood. Moreover, about half of the sites were willing to go beyond predesignated boundaries in order to qualify otherwise eligible properties. In such instances, block or building level data were typically used as the basis for determining eligibility.

Given the nature of the selection process, the source of data most commonly used in selecting or justifying target areas was census data on income (28 sites) and to a lesser extent, rent levels in 1980 (23 sites). This was supplemented in 13 sites with some review of locally collected data, typically existing planning studies or records. In one site, for example, income eligible tracts were matched against a listing of tracts in which Section 8 certificate holders resided, using the latter as an indicator of affordability. In 5 sites,

however, special data collection was conducted as part of target area selection or in an effort to get a better picture of market conditions. This included meetings with apartment associations (1 site); windshield surveys of physical conditions (2 sites); and reviews of newspaper listings (2 sites) to gather updated information on area rents.

Given substantial overlap with existing CD neighborhoods, areas with rental rehab projects also tended to be those in which other city programs were operating. Programs operating in the same neighborhoods as the RRP included owner-occupied housing rehabilitation programs (29 sites); street improvements or public works (28 sites); other rental housing rehabilitation programs (22 sites); code enforcement efforts (19 sites); and commercial development programs (19 sites). However, very few sites indicated any attempt to coordinate Rental Rehab with these other programs in a strategic sense. Exceptions included: three sites where the rental rehab areas or portions of them were considered "intensive treatment areas" in which a variety of programs were concentrated; one site where rental rehab was used in commercial areas along with a facade improvement program; another where weatherization and commercial programs were used along the with RRP; and, finally, one where some attempt was made to coordinate street and recreation area improvements with the RRP.

In the 22 sites where other rental rehabilitation programs were operating in the same neighborhoods as the RRP, 18 of the sites indicated no substantial difference between the types of properties treated by the programs. In only three cases was the RRP used for

different classes of properties. In two, the RRP programs were geared to properties that needed less work; in another, CDBG rental rehab was used mainly by non-profits, whereas the RRP included an investor-oriented component.

2.3.2 Types of Areas Selected for the Program

As noted above, 13 sites indicated that they had limited the Rental Rehab program to one or more target areas, which together represented some subset of all lower income areas in which projects might otherwise have been located (i.e., tracts with incomes below 80 percent of the SMSA median). The impact of this targeting is shown in Exhibit 2.7, which compares target areas in these sites to the set of potentially eligible neighborhoods. All data were obtained from the 1980 Census Tract Reports.

As is evident from the chart, the average "targeted" site restricted program eligibility to about half of all units located in lower income areas. This proportion ranged from about 12 percent in the most targeted site (which also expressed a strong neighborhood orientation to its program) to over 90 percent in the least targeted sites. However, comparisons based on tenure, race, rents, and various characteristics of the housing stock suggest that target areas as selected by the typical site do not differ substantially from low income areas generally. The only significant difference arose with respect to family income. While RRP neighborhoods have incomes that are relatively low (65 percent of the SMSA medians), they are somewhat above the incomes observed among the universe of tracts which meet the 80 percent income cut-off.

EXHIBIT 2.7

COMPARISON OF LOWER INCOME TRACTS AND
TARGETED AREAS FOR THIRTEEN SITES: 1980

	<u>Low Income Areas</u>	<u>Target Areas</u>
Population	360,987	174,819
Number of Households	132,355	63,569
% Black	31.7%	27.8%
% Hispanic	12.9%	13.7%
% Poor	23.0%	21.5%
% Elderly	21.2%	21.5%
% Renter Occupied	63.0%	59.6%
% Vacant	7.7%	7.3%
Structure Type		
% Single Family	25.6%	26.5%
% 2-4 units	28.1%	31.3%
% 5+ units	44.8%	41.2%
% Pre-1940 Rental Units	37.0%	41.0%
% Crowded	8.1%	7.7%
% Deficient ¹	11.6%	11.8%
Large Units		
% 2 Bedroom	34.6%	35.1%
% 3+ Bedroom	15.6%	14.9%
% of Units Renting Below the FMR	83.7%	83.1%
Average Gross Rent	\$210	\$211
Median Household Income	\$10,963	\$12,131
Median Family Income/ SMSA Median	54.5	64.6

1. Lacking complete plumbing or built before 1940 without central heat.

Given the relatively inclusive approach taken by the sites in identifying target areas, a more appropriate basis for examining Rental Rehab "neighborhoods" may be the areas in which projects are actually located. Exhibit 2.8 compares the characteristics of tracts with RRP projects (including commitments) to the characteristics of eligible areas as defined by sites. The latter include the designated target areas in the 13 sites that chose to target, and all eligible low income census tracts in the remaining 20 sites.

The overall characteristics of the two groups of tracts are again remarkably similar. Thus, there does not appear to have been a systematic effort on the part of communities to give preference to particular types of neighborhoods within their designated target areas. The data also suggest that the program is being targeted to the types of neighborhoods for which it was designed. As shown in column 2, about 85 percent of the rental units rented for less than the FMR in 1980. Family income was only about 65 percent of the local median, and a significant number of neighborhood residents were members of a minority group.

Individual sites varied considerably along these dimensions, but all sites targeted to low income areas where rents were relatively low. For example, the proportion of units with rents below the FMR ranged from 61 to 96 percent for tracts with RRP projects. Thus, in 1980 at least, the majority of units in project neighborhoods were affordable to low income households. While the ratio of neighborhood to SMSA income ranged from 43 to 109 percent, only 5 communities had ratios that exceeded the 80 percent guideline established by HUD. Four of

EXHIBIT 2.8

COMPARISON OF 33 CITY-DESIGNATED AREAS
AND ACTUAL PROJECT LOCATIONS: 1980¹

	<u>Eligible Areas</u>	<u>Areas With Projects²</u>
% Black	35.6%	41.1%
% Hispanic	14.7%	11.4%
% Poor	23.2%	22.6%
% Elderly	19.5%	19.9%
% Renter Occupied	60.6%	59.3%
% Vacant	6.7%	7.0%
% Recent Movers (Renters)	38.1%	38.6%
Structure Type		
Single Family	26.4%	26.9%
2-4	28.8%	28.5%
5+	43.5%	43.9%
% Pre-1940 Rental Units	36.2%	37.9%
% Deficient (All Units) ³	11.6%	12.0%
% Crowded	8.3%	7.7%
% 2 Bedroom Units (Rental)	37.3%	36.7%
% 3+ Bedroom Units (Rental)	17.7%	16.6%
% of Units Renting Below the FMR	84%	85%
Average Gross Rent	\$ 211	\$ 219
Median Household Income	\$12,026	\$12,200
Median Family Income/ SMSA Median	61.1	65.7

-
1. Data missing for Islip, N.Y.
 2. Includes both committed and completed projects.
 3. Lacking complete plumbing facilities or built before 1940 without central heat.

these were urban counties, who, due to the unique nature of their housing markets, qualified project neighborhoods on a smaller basis than census tracts. Finally, while the proportion of rental units with two or more bedrooms ranged from 5 to 84 percent, only 3 sites had located projects in areas where this fraction was less than one third. Two of these sites indicated that the lack of larger units had been a major impediment to their programs.

The census tract data are admittedly out of date and may not capture recent changes in the characteristics of target areas. As a result, we asked RRP program staff to rate the neighborhoods of the 125 sample projects as stable, declining or improving. In addition, our own inspection staff rated the condition of the housing stock in areas immediately surrounding Rental Rehab properties as "well maintained," "deteriorated," or "severely deteriorated." Exhibit 2.9 presents these ratings, which provide a more current, although admittedly subjective assessment of the types of areas in which RRP projects are located.

About 16 percent of the sample units were in neighborhoods that program staff rated as "declining." Forty-four percent were in "stable" neighborhoods, while 40 percent were in areas that were generally "improving." The latter classification is not synonymous with gentrification which, while difficult to measure, was not perceived to be a problem in the majority of the sample sites. Rather, the classification most likely reflects the fact that RRP neighborhoods are typically the targets of other public expenditures designed to upgrade urban areas. Similarly, based on the observations of our rehab specialists, the majority of RRP units (63 percent) appear to be located

EXHIBIT 2.9

RATINGS OF SELECTED RRP NEIGHBORHOODS¹

Program Staff Characterizations of RRP Project Neighborhoods

<u>Category</u>	<u>Percentage of all RRP Units</u>
Declining	16%
Stable	44
Improving	40
	<u>100%</u>

Field Inspection Staff Ratings of Housing Conditions
in RRP Project Neighborhoods

	<u>Percentage of all RRP Units</u>
Well maintained	63%
Deteriorated	34
Severely Deteriorated	3
	<u>100%</u>

1. 125 sample projects.

in areas where the stock is well-maintained. Only about 3 percent of the sample units were in areas with a severely deteriorated housing stock.

2.3.3 Impact of Neighborhoods on Program Performance

Exhibit 2.10 shows the relationship between the types of neighborhoods in which RRP projects are located and a site's performance on the different criteria established by HUD. Two different indicators of neighborhood conditions have been employed: the ratio of family income in census tracts with RRP commitments to the median family income in the SMSA; and the proportion of units in RRP neighborhoods that rented for less than the FMR. Again, both measures are based on 1980 Census data and thus, may be somewhat out of date.

The figures in the chart show a fairly strong relationship between neighborhood characteristics and program outcomes. While the proportion of very low income tenants served in place does not appear to vary with neighborhood income, other performance measures do. In particular, sites that had projects in neighborhoods with the lowest incomes had a higher proportion of three or more bedroom units and had rents that were significantly lower in relationship to the FMR. However, these same areas also had considerably higher public expenditures per unit, considerably lower leveraging ratios, and lower commitment and completion rates. Neighborhood rents also appear to influence program outcomes. Areas with the highest proportion of units below the FMR have the highest public costs, the lowest leveraging ratios, and the lowest commitment and completion rates. On the positive

EXHIBIT 2.10

PERFORMANCE MEASURES BY NEIGHBORHOOD INCOMES AND RENTS¹

	<u>Percent 3+ Bedroom</u>	<u>Percent Very Low Income Served in Place</u>	<u>Total Public Cost Per Unit</u>	<u>Public Cost as a Percent- age of Total Cost</u>	<u>Percent of Funds Committed</u>	<u>Ratio of Rents to FMR</u>	<u>Number of Sites</u>
Ratio of Neighbor- hood to SMSA Income							
Below 0.60	32%	33%	\$5,577	54%	53%	.84	14
0.61 - 0.80	21%	34%	\$4,698	50%	58%	.88	15
0.81 and Above	11%	34%	\$3,484	45%	82%	.89	5
Percent of Neigh- borhood Units Below the FMR							
Over 90%	27%	32%	\$6,611	60%	50%	.84	8
81% - 91%	23%	36%	\$4,390	51%	61%	.85	19
80% or Less	26%	29%	\$4,169	41%	65%	.91	7


1. Neighborhood data reflect average characteristics of tracts with RRP commitments.

side, the post-rehab rents of RRP projects in these areas are relatively low in relationship to the FMR.

Thus, while project location clearly has an impact on program performance, the impact appears to be mixed. Sites with properties in neighborhoods with lower-than-average incomes had a different set of outcomes than sites where neighborhood incomes were relatively high. However, when the different criteria are combined, overall performance was about the same. Relatively few sites have deliberately targeted to either higher or lower income areas, and relatively few have had much discretion in the selection of specific projects (see discussion below). As a result, these patterns probably reflect variations in local market conditions which influence program demand, rather than deliberate strategies on the part of grantees to concentrate activities in certain types of areas.

2.4 Outreach and Project Selection

The third important aspect of program design and development relates to the types of applicants that programs seek to attract and the marketing strategies that sites adopt to reach their intended audiences. The targeting of certain classes of properties is an inherently local process linked to local needs and objectives. Similarly, the selection of appropriate media to advertise and promote the program may vary based on a variety of factors, including geographic restrictions imposed by the program, the particular types of projects sought, ownership patterns, or the existence of local networks for disseminating information to suitable applicants. This section addresses these issues, beginning with a discussion of the types of owners sought by the



various programs and the extent to which outreach methods were geared to particular types of property owners.

2.4.1 The Target Audience

Among the 34 sample sites, fourteen (41%) indicated that they were trying to encourage the participation of particular owner types in their Rental Rehab Programs. Three of these were seeking experienced owners and sought them out through landlord associations and outreach through the PHA. Another three actively recruited larger scale developers. In one of these sites, the largest owners were invited to a program design conference, with most of the applications received subsequently flowing from attendees of this meeting. A second site in this group conducted a direct mail campaign to owners with certificates of occupancy for large multi-family buildings which were cited for code violations.

On the other hand, six sites said they were trying to encourage small scale "Mom and Pop" owners for the Rental Rehab Program. Four of these sites either targeted their marketing efforts geographically to areas where such owners were concentrated or addressed their newspaper ads to this specific audience. The remaining two sites in this group felt that the local RRP was inherently more attractive to smaller owners and that such owners would in large part select themselves for the program.

Finally, two sites sought other specific types of owners or properties for the program. One city attempted to encourage low-income owners by making clear in the program literature that it intended to give such owners priority. Another directed some of its mailings to

owners of brick (seismically deficient) buildings, which were targeted by the program and also offered a more generous subsidy to cover additional costs associated with the repair of these structures.

Cities that failed to focus on a particular owner or property type often did not do so out of a lack of priorities. Rather, because of a great deal of variation in local housing stock and/or a wide eligible area, some of these sites preferred to scatter their shots with a variety of marketing tools aimed at different sets of clientele in the hope that the program would engender a broad base of appeal.

While staff at many of the sites said they did not harbor expectations, many expressed surprise at the characteristics of applicants that eventually appeared. Especially noteworthy was the fact that many of them were small scale owners, or first-time investors with little experience in government programs. Twenty sites said these smaller, relatively unsophisticated owners comprised the bulk of their clientele. Eleven reported a mix, usually either of small, mid-sized, and large-scale owners, or just the two extremes. By contrast, three cities dealt almost exclusively with large-scale property owners, although only one of these cities had specifically attempted to attract this type of owner.

Some sites also experienced a number of "repeat" owners, rehabilitating two or more properties under the program. While in some cases a positive experience with one property led an owner to submit additional applications, in a few sites, a disproportionate share of the committed units were traceable to a few large owners. This result was

typically attributed to market conditions which discouraged participation except among owners with available cash to contribute. Several sites also drew on another group of traditional clientele: non-profits with previous experience under other city programs. Non-profits were active in 5 of the sample sites, and given relatively low production rates, often accounted for a sizable proportion of the project completions in these sites to date.

2.4.2 Outreach Methods

While some programs did gear their marketing efforts to particular types of owners, the majority adopted a broad range of techniques to advertise and promote the program. RRP marketing and promotional efforts in the 34 cities employed virtually every medium from newspaper advertisements to direct mail, to door-knocking, to heavy reliance on word of mouth. Degrees of emphasis differed among the sites as well. Some simply included material about the RRP in their standard information packets about all of their community development programs; others featured the Rental Rehab Program solo on local cable TV spots and public service announcements on radio. No city relied exclusively on one method and, in fact, over three-quarters of the sites experimented with between four and eight different media for disseminating information about the program.

As shown in Exhibit 2.11, direct mail campaigns, newspaper ads, and word of mouth -- this last from participating owners -- were among the most frequently relied upon means of advertising the program, and were also most frequently cited as particularly effective means of generating applications. There is, however, no apparent pattern by

EXHIBIT 2.11

OUTREACH METHODS EMPLOYED BY THE SAMPLE SITES
(number of sites)

<u>Type of Outreach</u> ¹	<u>Primary Method</u>	<u>Secondary Method</u>	<u>Not Used</u>	<u>Most Successful</u>	<u>Least Successful</u>
Newspaper Ads	10	16	8	7	5
Letters and direct mailings	17	10	7	10	6
Community meetings	9	19	6	5	4
Personal outreach to individual owners	8	7	19	3	0
Outreach through lenders	3	7	24	1	0
Outreach through PHA	9	12	13	2	1
Posters or pamphlets in public buildings	11	3	20	0	1
Public service announcements (Radio and TV)	8	5	21	4	3
Referrals through code enforcement	6	1	27	3	0
Word-of-mouth individual referrals from other owners	10	0	24	6	0
"Free" publicity - articles in newspapers and magazines	0	7	27	3	1

1. Multiple responses recorded.

which to predict the success of each medium. For instance, mass media approaches such as cable television and newspaper ads were cited by almost equal numbers of sites as both the most effective and the least effective means of promoting the program. While these methods may cast a wider net, they may also be less able to communicate a great deal about program requirements or benefits. Moreover, as at least one site discovered, they may not be appropriate for programs which also restrict the RRP to relatively small geographic areas. Success with more personalized methods, such as community or investor meetings, was also mixed and apparently depends a great deal upon the locally established network among program staff, neighborhood groups and owner associations.

2.4.3 Marketing and the Market

Just as sites had varying degrees of success with different marketing approaches, they also tended to emphasize different components of the program depending on local conditions and constraints. In loose rental markets for instance, the guarantee of an assisted tenant for at least one year (and potentially longer) at the prevailing FMR could be a major inducement for an owner to participate, and was stressed in many of these sites. The Section 8 component of the program also appears to have been a valuable commodity in rent controlled markets where approval for rent increases may otherwise be difficult to obtain.

By contrast, in some sites with tight markets, FMRs themselves may take on the appearance of quasi-rent control. To enhance the marketability of the program in one of these sites, staff emphasized the use of relocation and rental assistance to relieve overcrowding and reduce the attendant wear and tear on the properties, an approach that

proved to be quite compelling when coupled with a subsidy to undertake needed repairs.

Finally, a few sites highlighted other advantages of program participation, including technical assistance available from program staff. For example, at least one grantee attempts to enlist small scale owners and first-time investors in the program through the offer of extensive help in planning rehab jobs, running interference with contractors, and other activities which might deter inexperienced owners from undertaking repairs.

2.4.4 Owner Response

The types of owners attracted to in the Rental Rehab program and their motivations for participating are discussed in Chapter 5. From the perspective of the individual sites, however, a principal concern was the number of applications generated and the adequacy of these for maintaining acceptable production levels. At the time of the field visits, ten sites pointed to a less than adequate interest in their programs as measured in terms of numbers of applications. Several of these traced the problem to an administrative source -- lack of planning in marketing or delays in program start-up. Each of these sites said they intended to respond by stepping up marketing efforts. Two other sites traced the problem to fears -- real or perceived -- of excessive red tape on the part of owners who feel the cost of their time and aggravation is greater than the likely return. In response, these sites have dropped certain paperwork requirements such as procedures for public bidding and the purchase of title insurance for properties under a certain size.

Four, however, attributed their difficulties to market conditions: high cost economies which dwarf the size and importance of the subsidies, very high vacancy rates which increase the risk of investment and also make it difficult for owners to obtain private loans, and very low vacancy rates which enable the owner to command high rents even with the current condition of the property. To counteract market problems, respondents in some of these sites said they were considering implementing, as the ultimate marketing tool, the redesign of the subsidy mechanism itself. Precedents for this have already been set by a number of sites that adjusted their subsidies early on in the program when applications lagged.

2.4.5 Selection of Properties

As part of the Rental Rehab Program design, cities were asked to submit descriptions of the project selection procedures or preferences they intended to apply. Most of the sample sites developed formal selection criteria ranging in sophistication from simple checklists to rather complex point systems. Often the criteria stressed went beyond the program wide standards for rehabilitating large units, serving low income families, and minimizing displacement of existing tenants, and included mechanisms for favoring projects that met local objectives, as well. Some were designed to award more points to projects of a certain building size, that were owned by a low income person, or that were located in a priority area. Certainly such systems were devised in anticipation of substantial numbers of applications from which program staff could pick and choose.

Yet, the reality of project selection is quite different. The sites were surprisingly consistent in their approach to project selection and that this was so irrespective of the level of overall interest in the program they had been able to generate or the numbers of applications they actually received. All 34 sample sites indicated that applications were evaluated individually as they came in and not ranked or rated in competitive rounds. The individual treatment of proposed projects has meant that the selection criteria devised are less able and less likely to be formally and strictly applied.

The concept of "selectivity," though integral to the program, is difficult to pin down. While an attempt was made to collect information on project rejection and approval rates in each of the sites, such figures proved to be misleading. Especially in smaller sites, program staff were able to meet with nearly every inquirer to discuss the program, and it was often at this very early stage that a determination of the suitability of the project was made. Those projects that proceeded to the formal application stage were already a "go" in the eyes of all parties involved. By contrast, rejection figures reported by program staff in some of the sites include what were really drop outs or cancellations on the part of owners. Some of these owners may have failed to provide complete documentation, were unable to secure funds from a private lender, or simply decided that the subsidy offered was not sufficiently attractive. The intermingling of these categories with rejections on the grounds of ineligibility or unsuitability further renders these figures unreliable.

Certainly, program staff looked for certain characteristics in the project proposals they were considering. For example, when asked to indicate preferences, sizeable numbers replied that it is desirable for an owner to reside in the neighborhood where the project is located, or for the owner to have considerable equity in the project, or for the owner to be experienced in rehab. The lack of these features in an application, however, rarely -- if ever -- warranted the rejection of the project out of hand.

Program staff were also asked to indicate the degree of emphasis (high, medium, low) they have given in practice to various factors when evaluating an application. Overwhelmingly, the most important factors were those embodied in the national program guidelines: namely, the location of the project in an income-eligible area, the percentage of two or more bedroom units contained in the building, and the avoidance of displacing existing tenants. Significantly, less than half the sites expressed a preference for vacant or occupied buildings, or projects with a specific level of rehab needs, since most acknowledged the market rarely offered them a choice. Only seven sites indicated the degree of leveraging was an important factor in project selection.

Overall, then, the ability of sites to exercise selectivity or to base selection decisions on locally defined needs has been severely constrained to date. Several sites characterized their "selection" process as that of a "elimination process" in which the intense pressure to achieve adequate commitment levels means that any project that is

eligible and feasible is accepted. This is particularly true with respect to large units.

Despite waivers to do fewer two plus bedroom units, some cities encountered difficulty in meeting the large bedroom requirement and were forced to put applications for efficiencies and one bedroom units for the elderly on hold. In order to maintain commitment levels some sites now appear to be leaning towards the strategy of seeking out bigger properties and apartment complexes to stretch out administrative funds and maximize output.

2.5 **Administrative Processing**

Over the past decade, it has become widely recognized that the quality of program administration can have a sizeable impact on overall housing program efficiency and effectiveness. This is particularly true in a program like the RRP where subsidy amounts are comparatively small and administrative costs are likely to account for a larger share of total outlays. In this section, we review the way the RRP has been administered over its first two years of operation. We open with a discussion of concepts recently promoted by HUD to improve the efficiency of rehabilitation program administration. We then explain how the RRP is being administered and assess its administrative performance in relation to those concepts.

2.5.1 Framework: Hand-holding vs. Streamlining

Agencies responsible for operating publicly subsidized rehabilitation programs bear a substantial responsibility. The process is inherently complex and fraught with potentials for abuse. Charges of

improper use of funds in a number of rehabilitation programs in the 1960s heightened the concern of many agencies for tight control in all aspects of administration. This concern was also underscored by the "conventional wisdom" at the time: in effect, that private actors in the process (owners, contractors, lenders) were unable (or unwilling) to assume functional responsibilities in a manner that would support the public purposes of such programs. This outlook led to what is now termed a "hand-holding" approach -- one in which agency officials do as much as possible themselves and exercise tight oversight over any steps in the process that have to be done by outside parties.

Since the late 1970s, however, there has been a shift in emphasis. First, there was evidence that administrative costs had been much higher than had been suspected in many housing programs. The question was whether so much oversight was really cost-effective. Second, there was evidence that private owners, contractors, and lenders are quite capable of performing larger roles consistent with public objectives if programs are properly structured to enhance natural market incentives. Third, private business practices (quality control techniques, etc.) offered examples of much less staff-intensive approaches to preventing administrative mishaps.

An outgrowth of these factors has been the "streamlining" approach now advocated for rehabilitation programs. The Department (HUD 1985) defines streamlining as "the elimination of duplicative or unnecessary tasks within the rehabilitation process and/or delegation of appropriate duties to other responsible parties while maintaining essential controls." In this approach, the property owner assumes first

line responsibility for selecting a contractor, monitoring the contractor's work, and negotiating with lenders to finance the unsubsidized portion of the cost. The contractor prepares the work write-up (scope of work) and performs the rehabilitation consistent with its specifications (both to be overseen and approved by agency staff). Private lenders assess the project's financial feasibility and the owner's creditworthiness and service the loan. In reviewing RRP administration then, an important focus will be on the extent to which RRP sites have adopted streamlining and, to the extent we can identify them, the effects various administrative approaches have on administrative efficiency overall. Before we address that issue, however, we provide some background information on the way RRP programs were organized and staffed and on some limitations in the data base.

2.5.2 Overall Organization, Staffing, and Administrative Budgets

Perhaps the most important determinant of RRP administrative styles at this stage is the fact that the RRP is typically a small program, subsidiary to the main programmatic responsibilities of its implementing agencies. Normally, those agencies see themselves as broadly responsible for housing rehabilitation in their communities. In many cases, they operate one intake process to identify properties suitable for rehabilitation and then decide which of several available programmatic mechanisms to employ based on characteristics of the property at hand. The RRP is simply one of the available mechanisms. In our sites, considering funding to date, it was virtually never the dominant mechanism.

These circumstances largely explain the way the RRP operates within its implementing agency. Most of the staff who work on it do so on a part-time basis. In only three of our sample programs did the person identified as the RRP Program Director devote 90% or more of his or her time to RRP activities. In the larger programs, it was possible to assign some staff members (e.g., rehab specialists, inspectors) to work full-time on RRP projects, but this was the exception rather than the rule.

In almost all of our sample programs, staffing levels were too low to require any formal or specialized organizational structure within the RRP. Typically, one or two rehabilitation specialists performed all functions required to follow through on individual projects, occasionally obtaining specialized help from other branches of their agency or other city departments (e.g., financial analysis or inspections).

Data on Administrative Budgets and Staffing

None of the programs we examined maintained accounting systems that would permit fully accurate identification of RRP staff use and administrative costs. This is neither surprising or troublesome given the small size and subsidiary role of the RRP at this point (such accounting systems are expensive), but it means that much of our administrative analysis has to rely on the "best estimates" of program managers.

We asked them to provide three responses on these topics: (1) the size of their RRP administrative budgets; (2) a listing of all staff working on the RRP and the percentage of the time of each allocated to

RRP activities; and (3) an estimate of the amount of staff time required to perform each of the major RRP functions on a typical project. While the numbers they provided must be interpreted with caution, they did offer enough consistency to warrant reporting. We report findings on the first two of these responses below, and on the third, later in this section.

Administrative Budgets

Another factor explaining the lack of clear RRP administrative accounting is, of course, HUD's decision not to provide separate funding for RRP administration. RRP staff salaries and related costs, therefore, have to be funded from other sources, typically the local CDBG budget. Most agencies in our sample had no specific budget allocation for RRP administration -- funds for that purpose were an undistinguishable part of their overall CDBG administrative budget. In fact, nine of them (26%) were not willing even to estimate annual expenditures for administration.

Among the 25 programs that did have specific allocations or were willing to estimate them, RRP administrative budgets for 1985 ranged from \$6,000 to \$1.1 million. For most of those programs (72%), 1985 administrative budgets represented from 3% to 12% of their initial 1984-85 RRP subsidy grants (the median share was 8%). Only one program reported an administrative budget exceeding 30% of its initial grant. In almost all of these programs, virtually all budgeted expenditures went to cover personnel salaries and fringe benefits and some related share of overhead costs.

Staffing

All but two sites were able to provide listings of staff members showing the percent of their time each allocated to the RRP. In total, the reported staffing levels fell below 3 full-time-equivalents (FTEs) in 21 sites (about two thirds of the respondents). Only three sites reported more than 5 FTEs. FTEs per million initial grant dollars ranged from 0.8 to 8.1. For 19 sites, however, this ratio fell between 1 and 3 (median value 2.4).

2.5.3 Responsibilities for Administrative Functions

One way to assess the degree to which RRP agencies have streamlined administrative processing is to examine the way they have allocated responsibilities for required functions. The basic questions are: what functions have they delegated to owners and other private sector participants, and what steps do they continue to perform themselves? Allocations of primary responsibility for specific functions are presented in Exhibit 2.12.

1. Outreach and Intake Processing. Almost by definition, most of the functions in this phase of the process must be performed by the RRP agency. The table shows that this was the common practice. In all sites, outreach, intake/screening, and formal project selection functions were all handled by program staff. The only exception was one agency in which outreach activities were delegated to the city's public relations department. A move toward streamlining, however, is illustrated by one function in this group: collecting data on pre-rehab tenants. In 20 sites (59%) owners were assigned responsibility for providing this data.

EXHIBIT 2.12

RESPONSIBILITIES FOR STEPS IN ADMINISTRATIVE PROCESSING
(Number of Sites)

	<u>Prog Staff</u>	<u>Other Dept</u>	<u>PHA</u>	<u>Owner/ Contractor</u>	<u>Lender</u>	<u>Not done</u>
1. Outreach/Intake Processing						
Outreach to owners	33	1	-	-	-	-
Intake/initial screening	34	-	-	-	-	-
Survey pre-rehab tenants	12	-	2	20	-	-
Formal property selection	34	-	-	-	-	-
2. Initial Property Inspection						
Inspection	32	1	-	1	-	-
3. Scope of Work/Select Contractor						
Prepare scope of work	18	1	-	15	-	-
Approve scope of work	30	2	-	2	-	-
Obtain bids/select contractor	3	-	-	31	-	-
Determine subsidy amount	34	-	-	-	-	-
4. Financing						
Arrange private financing	2	-	-	32	-	-
Assess financial feasibility	29	-	-	-	5	-
5. Construction Management/ Payment						
Progress inspection/ payment approval	33	1	-	-	-	-
Final inspection/approval	30	3	1	-	-	-
6. Tenant Assistance						
Post-rehab tenant survey	8	-	15	11	-	-
Certify/issue certificates	3	-	31	-	-	-
7. Service loans						
	21	1	-	-	5	7

2. Initial Property Inspection. Program integrity generally demands that this function be performed by a government official and this was in fact the practice in all but one of the programs in our sample. Although HUD literature on streamlining recommends against it, one program allowed the owner's contractor to complete the inspection, using detailed forms and guidelines provided by the RRP staff.

3. Preparing the Scope of Work and Selecting the Contractor. HUD streamlining literature recommends that the scope of work be prepared by the owner (or contractor) based on the initial inspection report and subject to later review by the program staff. Only 15 of the sample programs (44%) followed that advice. Several of the agencies that prepared the scope of work themselves, however, said that they did so in the interests of efficiency. They argued: (1) little staff time was needed to prepare the scope since it required only a minor rephrasing of the inspection report; and (2) the scope prepared by the staff gave the owner very clear signals on allowable repairs.¹ By contrast, the sample programs overwhelmingly endorsed the streamlining approach by delegating the responsibility to the owner for obtaining bids and selecting the contractor. Only three RRP agencies retained that function. Not surprisingly, approving the scope of work and determining the subsidy amount were retained as government functions in all sites.

1. These sites usually permitted some changes to the first draft in negotiating with the owner, but felt much more time would have been required for negotiations if the owner -- typically not that well informed about program rules or the rehab process -- had tried to prepare the work write-up himself.

4. Financing. In all but two of the sample programs, owners were responsible for securing financing for that portion of the cost not covered by the RRP grant. However, several other programs assisted the owners in that task, often finding other public subsidy funds for the purpose. The data show that almost all RRP agencies retained responsibility for analyzing project financial feasibility, but in five of the sites, private lenders subsequently performed the underwriting tasks related to project loans.

5. Construction Management and Progress Payments. Progress inspections and payments were handled directly by the RRP staffs in all but one sample program, and in that case these activities were delegated to a closely related agency. Final inspection also consistently remained a government function, handled in one case by the PHA, in two by delegation to the city's building inspection department, and in all others by the RRP staff.

6. Tenant Assistance. The tasks of certifying tenant eligibility, issuing certificates, and making subsequent tenant subsidy payments were universally assigned to the PHA (the three cases where the "program staff" handled these functions were those in which the PHA served as the RRP agency). Responsibility for the collection of post-rehab tenant data was the responsibility of the PHA or RRP staff in 68% of the sites and the owner in the remaining 32%.

7. Servicing Loans. Responsibility for servicing RRP related loans and/or compliance monitoring was typically performed by city staff or a related government department. In 5 sites lenders performed all loan servicing functions.

Overall, these data indicate that the RRP has moved toward a relatively streamlined approach to program administration. In almost all sites, the owner was responsible for obtaining bids, selecting the contractor, and arranging financing for that portion of the rehab cost not covered by RRP funds. Even though a significant share of the RRP agencies retained responsibility for preparing the scope of work, most did so because they believed it was a more efficient practice. The question remains, however, as to how much this apparent shift toward streamlining really contributed to administrative efficiency. To answer this question, we can examine what the RRP agencies said about their approach to streamlining and their estimates of staff time required to complete a typical project.

2.5.4 A Harder Look at Streamlining and Administrative Efficiency

As a part of the data collection, RRP managers were asked explicitly whether they attempted to promote streamlining in their operations. Sixty-two percent responded positively, but when we examined these responses in relation to other indicators we found that many who said they promoted streamlining had done so in only a minor way and others who responded negatively to the question had in fact made notable efforts to improve administrative efficiency. A more useful indicator was managers' responses as to the amount of time their staffs devoted to helping owners in various phases of the process. Specifically, they were asked whether they spent considerable, some, or no time to helping owners in: (a) preparing the scope of work; (b) obtaining financing of the unsubsidized portion of the cost; (c) seeking bids and selecting contractors; (d) managing the rehabilitation process;

and (e) dealing with tenant issues. We assigned point scores to their responses and averaged them. A score of 100 was assigned if the staff indicated that they devoted "considerable" time to helping owners on one of these functions; a score of 50 was assigned if they said they devoted "some" time, and 0 was assigned if they devoted "no" time. The resulting average scores were fairly evenly distributed, slightly weighted toward the lower (more streamlined) end of the scale:

Top third of the sites	:	more than 50 points
Middle third of the sites:		31-50 points
Lowest third of the sites:		30 points or less
Median score	:	50 points

Three sites had scores of 100, and three had scores of 10, and none had a score of 0. Individual site scores were generally corroborated by data on the allocation of functional responsibilities; e.g., those agencies that delegated few or no functions to the owner or other private actors had among the highest scores on this scale. Those same agencies said that they did not try to promote streamlining and, in responses to other questions about administration, most of them openly endorsed a hand-holding approach as necessary to meeting program objectives. We also ranked the sites according to the total number of staff hours managers said they employed to complete a typical project. Here, results were quite varied ranging from 9 person hours to 222 person hours.

Top third of the sites	:	70 or more person-hours
Middle third of the sites:		26-64 person-hours
Lowest third of the sites:		24 person-hours or less
Median time	:	31 person hours

Without the benefit of detailed time-allocation studies, estimating time requirements for a typical project is a difficult task. We had expected wide variations in estimates across the sites. Actually, however, the distribution by project person hours closely matched the pattern of scores on the assessment of effort in helping owners noted above. For example, 9 of the 11 sites that were in the top third according to the assistance index were also in the top third according to project person-hour requirements. All but three sites in the lowest third according to the assistance index were also in the lowest third according to person-hour requirements. It is convenient to think of agencies in the top third according to the assistance index as "hand-holding agencies", those in the middle third as "intermediate agencies", and those in the lowest third as "streamlined agencies". Using this terminology we examine more detailed breakdown of estimated staff time requirements in Exhibit 2.13.

The table shows averages of the estimates for the three groups (in contrast to the medians noted earlier). Clearly, there are marked differences between the groups and they are in the expected directions, i.e., handholding agencies devote considerably more staff time per project than streamlined agencies. Of more interest here, however, is the comparison of time requirements for different functions. The table shows there are marked differences between groups by these measures. Several conclusions stand out:

EXHIBIT 2.13

ESTIMATED STAFF HOURS REQUIRED
FOR MAJOR ADMINISTRATIVE FUNCTIONS ON A TYPICAL PROJECT

	Median hours	Mean Hours			
		Total	Hand- hold	Inter- mediate	Stream- line
1. Intake/processing	3.3	5.1	10.6	3.6	2.4
2. Initial property inspection	2.3	4.7	13.9	2.5	1.9
3. Scope of work/ contractor selection	4.0	4.3	5.9	4.6	2.2
4. Financing	.5	4.8	15.9	.5	.3
5. Constr. management payment	15.0	27.7	57.1	24.6	15.6
6. Tenant assistance	2.0	10.0	10.1	13.5	2.4
7. Other administrative	2.0	3.4	6.8	2.9	2.0
Total	30.8	60.0	120.3	52.2	26.8
Sample Size	34	34	11	10	13

- o Differences in the totals are not explained by only one or two functions. In virtually all functions, estimated time requirements are higher for hand-holding agencies than intermediate agencies and higher for intermediate agencies than streamlined agencies.
- o The largest contrast among functions occurs with respect to securing financing. This function accounts for 13% of the total time requirement for hand-holding agencies but for only about 1% for intermediate and streamlined agencies. There is also an important contrast of the same nature in the initial inspection function. Hand-holding agencies spend 12% of their time on that activity, compared to 5% for intermediate agencies and 7% for streamlined agencies. Strangely, tenant assistance accounts for a much larger share of the total for intermediate agencies (26%) than for hand-holding or streamlining agencies (9%).
- o For all groups, by far the largest share of time is required for the construction management and payments function (47% for hand-holding and intermediate agencies, 58% for streamlined agencies).

By definition, these estimated time requirements are very crude. Nonetheless, they suggest two implications for policy. First, some agencies seem to be able to administer the RRP with much lower staff requirements than others. Efforts to promote administrative efficiency in hand-holding agencies could have a substantial payoff. Second, the streamlining concept should deal with methods of performing functions retained by RRP agencies as well as simply the delegation of more functions to private actors. It would appear that a sizeable reduction in staff time requirements for the construction management and payments function, in particular, could have a marked impact on administrative costs.

These positive findings for streamlining hold up, of course, only if streamlining agencies are also securing adequate quality standards in their rehabilitation projects. In fact, data presented in Chapter 6 suggest that some agencies may have gone too far: delegating

program functions to owners without retaining enough control to assure effective rehabilitation. Others, however, have been able to streamline and yet retain sufficient control over rehab quality. Assuming that administrative streamlining is generally associated with good program performance overall, how much of a difference does it make in overall program costs? While they are very crude, the estimates we have obtained on budgets and staffing permit at least some rough approximations to respond to this question.

For the 23 sites that provided reasonable estimates on both budgets and salaries, the median total budget per FTE was \$32,603 per annum, or about \$17 per person hour. (For these sites, annual costs per FTE ranged from \$15,000 to \$59,000). Applying the \$17 hourly average administrative cost to the average time requirements in Exhibit 2.12 (and assuming the 5.5 unit average project size in our sample) yields the following results:

	<u>Admini- strative Hours/ Project</u>	<u>Admini- strative Cost/ Project</u>	<u>Admini- strative Cost/ Unit</u>
All agencies	60	\$1,020	\$185
Hand-holding agencies	120	\$2,040	\$371
Intermediate agencies	52	\$ 884	\$161
Streamlining agencies	27	\$ 459	\$ 83

An average administrative cost of \$185 per unit represents 4.4% of our sample's median \$4,241 per unit RRP subsidy. This amount is consistent with our earlier finding that, for 72 percent of the sites that reported administrative budgets, those budgets fell between 3 percent and 12 percent of initial RRP grants. The data indicate, therefore, that administrative costs run about 9 percent of the average

RRP project subsidy in hand-holding agencies, compared with about 2 percent in streamlining agencies.

2.5.5 Administrative Approaches and Program Performance

Since they devote so much less staff time to program administration, some might have expected the streamlined agencies to be less effective in achieving overall program goals. This, however, proved not to be the case. In fact, agencies that chose a more streamlined approach to the program did relatively well with respect to most of the RRP performance measures defined in Chapter 1 (Exhibit 2.14). Streamlined agencies attained the highest production levels, as measured by both commitment and completion rates. Interestingly enough, the hand-holding agencies came in second on this score, while the intermediate group lagged behind. The highest proportion of two bedroom units was also achieved by the streamlined agencies.

The only rating on which the streamlined agencies scored significantly below the hand-holding agencies was the percent of completed units that retained their pre-rehab low income tenants. However, this lower performance on this score reflects the fact that they developed projects with relatively high pre-rehab vacancy rates (47 percent for streamlined agencies versus 29 percent for other sites). It does not reflect a higher rate of mobility among pre-rehab tenants, which could be evidence of displacement. In fact, mobility rates in the streamlined agencies were marginally below the rates observed in other areas (27 versus 30 percent).

EXHIBIT 2.14

INFLUENCE OF ADMINISTRATIVE APPROACH ON PERFORMANCE ¹

	<u>Stream- lined</u>	<u>Inter- mediate</u>	<u>Hand- holding</u>
Proportion 2BR units	.85	.71	.67
Proportion 3BR units	.26	.24	.24
Proportion of low income households retained	.28	.33	.40
Public \$ per unit	5,100	4,600	5,100
Leveraging	.50	.51	.52
Commitment rate	.66	.52	.60
Completion rate	.24	.11	.14
Ratio of rents to FMR	.87	.89	.83
Sample Size	13	10	11

1. Weighted to reflect the administration of the average grant dollar.

Exhibit 2.15 shows that streamlined and hand-holding agencies had a quite different pattern of performance when production and leveraging goals are considered together. While the hand-holding agencies achieved above average production rates, many apparently did so at the expense of leveraging. The highest concentration of hand-holding agencies appears in the high-production, low-leveraging category. The highest concentration of streamlined agencies, however, appears in the high-production high-leveraging category. While the two types of agencies achieved about the same leveraging rate overall, the streamlined agencies were much more likely to achieve both production and leveraging objectives.

2.5.6 Recordkeeping, Monitoring and Reporting

Detailed information on properties which receive Rental Rehabilitation funding is primarily located in individual project files maintained by the grantee. These typically contained extensive documentation, including owner applications and financial data, inspection summaries, a costed scope of work, payment requests and approvals, loan documents, and other correspondence. In addition, most sites maintained processing logs — either manual or on PC. These were used to review the status of individual projects, schedule processing steps, and monitor production levels or other key aspects of program performance, such as the proportion of large units committed to date.

Standardized data on Rental Rehab properties are also collected and reported into HUD's Cash/Management Information System (C/MI). The system is designed to serve two functions. First, the C/MI collects two waves of data on each project funded under the program. A Pre-Rehab

EXHIBIT 2.15

ADMINISTRATIVE APPROACH, PRODUCTION, AND LEVERAGING
(Percent of Sites)

	<u>Total</u>	High Prod. High <u>Lev.</u>	High Prod. Low <u>Lev.</u>	Low Prod. High <u>Lev.</u>	Low Prod. Low <u>Lev.</u>	<u>N</u>
All sites	100%	21%	29%	29%	21%	34
Administrative Approach						
Hand-holding	100%	9%	55%	27%	9%	13
Intermediate	100%	18%	9%	36%	36%	10
Streamlining	100%	33%	25%	25%	17%	11

report is submitted immediately after project set-up, providing basic information on: the characteristics of the project and its owner; estimated rehab costs; the initial RRP fund request; and a record for each unit in the project describing the number of bedrooms, the initial rent and occupancy status, and the tenant's race, income, size and assistance status. The Project Completion Report, submitted at 75 percent occupancy or 90 days after final draw-down, provides an equivalent post-rehab tenant record for every unit, as well as final data on rehab costs and the sources and amounts of funds used to support the rehab.

The CM/I data base is intended for use as an evaluation tool, as well as for grant adjustments based on performance criteria developed by the Department. In addition to providing tenant and property data, the C/MI is used to control electronic fund transfers to program participants. Projects must be "set up" in the system to receive funds and permit drawdowns. As an incentive for timely data submission, failure to submit required reports can trigger a hold on project funds or future set-ups.

As a cash management system, the C/MI appears to have worked quite well. Despite complaints voiced by a few sites about delays in receiving funds, the system appears to offer an efficient approach for disbursing funds and exercising management control. As an information system, the C/MI also provides HUD with a useful tool for monitoring program progress and, with a few exceptions, provides an accurate overall picture of how the program is operating. Those data problems that do exist are relatively minor and should be fairly easy to

resolve. In fact, on-going HUD efforts to screen data, clarify reporting instructions, and request amended reports may have already improved the data since the first wave of completions which are used as the basis for this report. (For a more detailed discussion of C/MI accuracy, see Appendix B.)

The C/MI appears to be highly reliable with respect to project level data, including the sources and amounts of funds that have been used to support the rehab. Although we found some minor deviations between final rehab costs as reported into the system and actual project costs as reflected in contract documents, differences were extremely small, averaging about one percent in our sample of 125 projects. Similarly, information on sources and amounts of funds showed little deviation.

By contrast, unit/household records contained in the C/MI included numerous inconsistencies between the pre- and post-rehab listings, and required a substantial number of corrections based on information collected in the field. A major cause appears to be the source of the data used to complete the C/MI form. The pre-rehab listing was typically obtained from owner-supplied data usually provided in applications. Post-rehab data was usually drawn from several sources, including the PHA for assisted tenants and the owner or program staff for unassisted tenants. There appeared to be little effort devoted to comparing pre- and post-rehab listings to identify and resolve the resulting anomalies.

While we did not attempt to verify tenant characteristics directly, we made such corrections as were possible based on PHA and

program records, as well as interviews with project owners. Despite the frequency of such changes, the overall impact was again extremely small. Breakdowns by income group, family composition and other characteristics as reported on the original and corrected versions of the C/MI were virtually identical, suggesting that the C/MI provides an accurate portrait of the characteristics of the households being served. The only exception related to project rents, which tend to be understated. Although sites were instructed to record gross rents, contract rents were often used. When the CM/I data were corrected to include utilities, reported post-rehab rents rose by about 7 percent.

Apparently, staff in a number of sites have misinterpreted the type of rents to be reported. Significantly, C/MI reports are almost always completed by rehab staff who are less familiar with these distinctions than their PHA counterparts. Nevertheless, given the weight HUD places on unit affordability (measured by gross rents in relation to the FMR), HUD may want to continue to highlight this problem in communications with grantees to ensure that future reporting is consistently based on gross as opposed to contract rents.

2.6 Site Perceptions: Objectives, Obstacles, and Assessments

The earlier parts of this chapter have concentrated on describing how the RRP has been implemented in various localities. In this section, we report on the perceptions of agency managers about the program. We open by reviewing the way they see their objectives and priorities in program operation. We then note various obstacles and needs for improvement that they feel must be dealt with to improve local

program effectiveness. Finally, we look at the types of tradeoffs sites have faced in implementing their RRP programs.

2.6.1 Objectives and Priorities

In any program with several legitimate objectives, it is often difficult to assess comparative priorities reliably in the abstract. One cannot expect what managers say about their objectives and concerns to be fully consistent internally or consistent with their priorities as observed in actual practice. Such inconsistencies did emerge as we asked RRP managers about their goals. Nonetheless, their responses offer several useful insights.

We first asked the managers to rank the importance of three major RRP goals: increasing the supply of standard units, assisting eligible tenants, and upgrading neighborhoods. Just over two-thirds of the sites ranked the supply objective first (Exhibit 2.16). This objective was ranked first by the majority in each group (classified by commitment rate), but interestingly enough, it was rated first more frequently among sites that ranked in the lowest third (81%) than among those in the highest production group (55%). The share citing tenant and neighborhood objectives was much higher among the high commitment sites than the low commitment sites.

We next asked the managers the priority they assigned a number of more detailed program objectives. Several findings are of interest:

- o With surprising consistency in all groups, avoiding displacement was the most frequently cited high priority (82%-92%). A substantial number of the sample sites indicated that they preferred to accept vacant properties for the RRP as a means of avoiding displacement — this in spite of the presumably higher costs associated with vacant units and the

EXHIBIT 2.16

**STATED AGENCY RRP OBJECTIVES AND PRIORITIES
(Percent of Sites)**

	<u>Agencies by Production Rate</u>			
	<u>Total</u>	<u>Top Third</u>	<u>Middle Third</u>	<u>Lower Third</u>
Primary Objective				
Increase supply of standard units	68%	55%	67%	81%
Assist eligible tenants	18%	18%	25%	9%
Upgrade neighborhoods	15%	27%	8%	9%
Rated as High Priority				
Rapid program start-up	38%	45%	50%	18%
Rehabbing largest number of units	26%	18%	33%	27%
Avoiding displacement	85%	82%	92%	82%
Serving larger families	35%	36%	25%	18%
Keeping long term rents below FMR	21%	18%	25%	18%
Maximizing initial occupancy by low and very low income tenants	62%	55%	75%	55%
Arresting neighborhood decline	59%	64%	50%	64%
Maximizing leverage of private funds	29%	18%	33%	36%
Minimizing administrative cost	38%	45%	33%	36%

lower scores on "serving in-place tenants" that result from this strategy.

- o The second most frequently cited priority, fully consistent with program objectives, was maximizing initial occupancy by low and very low income tenants (62%). It is not unexpected at this stage that this objective would be a more immediate priority than its longer term equivalent: keeping long term rents below FMR (21%).
- o Arresting neighborhood decline was rated a high priority with unexpected frequency (59%) considering its comparatively low placement in the ranking of primary objectives and the non-restrictive targeting approaches adopted by many of the sites.
- o While most sites said that increasing the supply of standard units was their primary long-term objective, comparatively few (38%) considered rapid start up in doing so a high priority. Not surprisingly, this objective was much more frequently cited by those who were achieving it (high and mid-level production groups) than those who were not.
- o Minimizing administrative cost was considered a high priority by 38% of the sites. It was cited more often by the high production group than either the mid or lower groups. (As would be expected, most who saw this as a priority were streamlining agencies as defined in Section 2.7).
- o Finally, comparatively small numbers gave high local priority to other HUD rating factors such as serving larger families (35%) or maximizing leveraging of private funds (29%).

2.6.2 Obstacles to Performance

The majority of the managers in our sites (56%) perceived no obstacles at present to the effective local operation of the RRP. This conclusion was reached with substantially greater frequency among those with high production rates (91%) than those who were far behind in with respect to production (18%). For sites that did perceive obstacles to program process, problems identified were as follows (see Exhibit 2.17):

- o 3 sites (9%) indicated that their subsidy mechanism was not attractive enough. All employed repayable loans and two noted that political barriers had prevented them from adopting a more liberal approach.

- o 5 additional sites (15%) also said their major problem was attracting owner interest, but could not specify the cause.
- o 4 sites (12%) identified obtaining private financing as an obstacle, either because of difficulties in getting private lenders to participate or because owners were slow in obtaining financing on their own.
- o 3 sites (9%) indicated that HUD requirements pertaining to the proportion of large units was an obstacle to production.
- o 7 other sites (21%) cited various other problems, including difficulty in attracting low income owners (targeted by the program) and restrictions due to neighborhood targeting. The site with the lowest production rate in the sample indicated that cumbersome city loan processing requirements were a major factor.

2.6.3 Needs for Improvement

A significant number of program managers identified needs for improvements in their own staff capacities (Exhibit 2.17). Strongest in this regard was the need to improve management expertise (35% of the sites), followed by needed improvements in technical rehab skills (24%), and skills in financing and subsidy determination (21%). It is noteworthy that sites with the highest production rates were generally the most self-critical; i.e., more frequently identified needs to improve their own capacities.

2.6.4 Trade-offs in Implementation

As suggested throughout this chapter, Rental Rehab sites were faced with important trade-offs in program design and administration. In some cases, sites were required to trade off locally defined needs against national program requirements (e.g., a perceived need for downtown, small unit, or SRO housing vs. the RRP's emphasis on large unit production). In other cases, programs were in the position of trading

EXHIBIT 2.17

OBSTACLES, NEEDS FOR IMPROVEMENT, PROGRAM ASSESSMENT
(Percent of Sites)

	<u>Agencies by Production Rate</u>			
	<u>All Sites</u>	<u>Top Third</u>	<u>Middle Third</u>	<u>Lower Third</u>
Perceived Obstacles to Program Progress *				
None	56%	91%	58%	18%
Subsidy mechanism not attractive	9%	-	8%	18%
Other problems attracting owners	15%	-	17%	27%
Private financing problems	12%	-	17%	18%
Proportion 2+ BR requirement	9%	9%	8%	9%
Limited staff	9%	9%	8%	9%
Others	21%	9%	-	55%
Need Improvement in Expertise				
Program design	6%	-	-	18%
Program management	35%	45%	25%	36%
Technical rehab skills	24%	18%	17%	36%
Financing and subsidy determination	21%	27%	25%	9%
Overall Program Assessment				
Very satisfied	59%	82%	67%	27%
Somewhat satisfied	32%	18%	17%	64%
Somewhat dissatisfied	9%	-	17%	9%
Very dissatisfied	-	-	-	-

1. Includes multiple responses.

off one RRP performance measure (e.g., attaining maximum production levels) against others (e.g., minimizing the use of public funds). In general, it appears that the pressure to commit grant funds as rapidly as possible figures strongly in the minds of program administrators, and achieving acceptable production rates operated as a trade-off against a variety of other program objectives.

Obtaining a Payback of RRP Funds

As described in Section 2.2, as of mid-1986, half of the sample sites offered the RRP subsidy in a non-repayable form, while the remainder offered direct or deferred loans. Between program inception and the site visits, seven sites instituted major changes in their subsidy approach by either moving from a repayable subsidy to a grant-like mechanism or by reducing interest rates on their loan offerings. In all cases, the switch was made in response to low levels of program applications, indicating that a more generous subsidy would be required to induce owner participation. While the trade off may have been less explicit in other sites, it is apparent that many sites weighed the immediate attractiveness of a forgivable subsidy against a desire (and in some case a political need) to obtain a return on these funds. In fact, desire to generate a payback for future use motivated one of the sample sites, which was also concerned about cutbacks in CDBG allocations, to switch quite recently from a grant to a loan regardless of the impact on commitments.

Leveraging

The Rental Rehab program promotes leveraging both by the limitation on the proportion of costs which may be covered with RRP

funds (50%) and encouragement for the use of gap financing analysis to ensure that the subsidy provided by the program is the minimum required to make projects feasible. As shown in Section 2.2, gap financing approaches were little used in the program. While this choice restricted the sites' ability to tailor subsidies to individual project needs, sites presumably felt that to do so would be administratively burdensome and would risk reducing owner participation.

A substantial number of sites also opted to supplement RRP grants or loans with CDBG funds in order to produce certain types of projects (particularly those with non-profit sponsors) or to make the program more attractive to property owners. Significantly, maximizing private leveraging was not a major priority among the local programs, despite its traditional use as a measure of program success and its explicit use in HUD performance criteria for the RRP.

Neighborhood Targeting

As described in Section 2.3, the RRP is, on the whole, a loosely targeted program. Beyond restricting the RRP to eligible low-income areas, relatively few sites sought to target the program to particular neighborhoods or other subsets of their eligible areas. Moreover, as the program progressed, eight of the sample sites were forced to expand their initial target areas in an attempt to broaden the base from which participants could be recruited, and three of the sample sites noted this as an important program trade-off. At least to date, then, the program's emphasis on careful neighborhood selection has not really been tested. The need to maintain adequate commitment levels has

means that applications have been accepted from virtually any part of the jurisdiction as long as program regulations are met.

Selectivity in Project Approval

Perhaps the most frequently mentioned tradeoff by local program staff was maintaining production levels versus the exercise of selectivity in committing projects to the program. As described in Section 2.4, most sites had established formal selection criteria for the RRP, including, in some cases, elaborate point systems for ranking projects against one another. However, as the program got underway, such systems were universally abandoned in favor of a first-come, first-served approach for projects that met basic acceptability criteria. The dearth of substantial interest in the program in some sites (whether due to the unattractiveness of the subsidy or to inadequate marketing), coupled with a pressure to commit funds, led to a "take what you can get" approach and less emphasis on local preferences that might otherwise have come into play. In fact, the only strong factors influencing project selection decisions were the unit sizes proposed and the need to avoid displacement. (Only one site suggested that it had accepted higher levels of displacement in order to maximize production.)

Large Unit Production

The requirement that 70 percent of all RRP units contain two or more bedrooms appears to have been an important constraint in a number of programs. Overall, 12 sites suggested that the large unit requirement had slowed the program down, and three considered it to be a principal obstacle to program progress. It should be noted, however, that as of mid 1986, only seven sites had been unsuccessful in

committing the required proportion of larger units. Nevertheless, many sites indicated that they had difficulty in attracting substantial numbers of two-bedroom units into the program while additional one-bedroom units could easily have been committed.

In general, the sites appeared to treat the large unit requirement as a given, making concerted efforts to stay at or near the required levels, and, in some cases, turning small unit applications away. One site, which ultimately obtained a waiver reducing the large unit requirement to 50 percent, operated under a 3-month moratorium during which the HUD field office would not allow any additional commitment of studios or one bedroom units. Another site operated under a similar moratorium, though apparently self-imposed. Finally, a third site, which allocated portions of its grant award to different sized units, had exhausted all funds reserved for small units at the time of the site visit.

Administrative Tradeoffs

As shown in Section 2.5, sites have adopted varying degrees of streamlining in their programs both with respect to the allocation of various functions and the amount of staff time devoted to key program activities. This can make a substantial difference in administrative costs, and is possibly of greater importance in the RRP, given that no administrative funds are provided. While a few agencies, specifically sought to minimize administrative costs under the program, and adopted a more streamlined approach for this reason, it is probable that the majority merely adopted the most comfortable approach based on their previous experience and the types of owners they expected to

participate. Significantly, however, several of the participating sites suggested that inadequate staff capacity was a problem in their program, and a number of HUD field office monitors also pointed to a need to boost the number of FTEs devoted to the program in particular sites in order to meet production goals.

2.7 Summary and Conclusions

The Rental Rehabilitation Program is typically administered by a city or county rehabilitation agency working in conjunction with an independent PHA. City or county actors have generally taken the lead in designing local programs and in carrying out most activities related to the selection and rehabilitation of the RRP properties. Not surprisingly, there was substantial variation among the sample sites with respect to their previous rehab experience and their approaches to implementing the RRP. However, experience -- both in terms of output under CDBG rehab programs and participation in the RRP Demonstration -- were not related to a site's performance under the RRP. Similarly, administrative factors, such as agency type or the extent to which programs had adopted a streamlined delivery approach, had little impact on performance.

In contrast, the type of subsidy offered by the sites appears to have a substantial impact on program performance. Seventeen sites offered non-repayable subsidies, either grants or forgivable deferred payment loans (DPLs). Fourteen delivered the subsidy as a repayable loan, while three sites offered both forgivable and repayable forms. Significantly, very few sites attempted to minimize subsidies through the use of gap financing techniques, variable loan terms, or the

imposition of a subsidy maximum lower than the 50 percent of cost of \$5,000 per unit cap established by the program. The sites' failure to adopt gap financing techniques or otherwise attempt to gear subsidies to the needs of individual projects suggests an important trade-off between leveraging goals and the need to maintain high production levels through the offer of a simple and attractive subsidy form. In general, sites appeared to place less emphasis on leveraging than might have been expected. Indeed, the majority of sites (21) offered additional public funding to at least some of their Rental Rehab projects.

The form in which the RRP subsidy was delivered significantly affected commitment rates. Sites offering non-repayable subsidies typically show higher commitment rates, regardless of the type of market in which they are operating. However, market factors also appear to play an important role, with sites operating in tight markets showing generally higher commitment rates than those in loose markets. Tight markets, however, are also associated with the lowest leveraging ratios, suggesting that programs in these areas have purchased at least some of their production through the use of other funds to supplement Rental Rehab dollars. It is also important to point out that the Rental Rehab program provides localities with ample flexibility to adjust their subsidies to changing market conditions and owner demand. Over the two-year period covered by this study, ten sites took advantage of this opportunity, with nine of these opting to convert to a more generous subsidy approach. Again this reflects a trade-off between the goals of leveraging and/or obtaining a payback on RRP funds and a desire to

maximize commitments through the provision of a more attractive subsidy offer.

Apparently, the need to achieve high commitment levels also contributed to a reluctance on the part of the sites to select narrowly defined target areas. The majority of the sites designated eligible areas on the basis of HUD regulations without further attempts to focus the program, and a number of sites expended their target areas over time in order to broaden the base from which owners could be recruited. Five sites did not designate eligible areas at all, but instead qualified projects as applications were received based on project- or block-level data.

Site approaches towards project selection were similar to those towards neighborhood targeting. Program descriptions and other early documentation typically contained explicit preferences for the types of owners/projects sought, and occasionally contained rather complex scoring systems for use in project selection. In practice, however, projects were approved on a first-come, first-served basis with little regard to stated preferences. The only factors that appeared to play a major role in project selection were the need to avoid displacement and the size of the units to be rehabilitated. Given program standards for the proportions of two- and three-bedroom units to be produced, projects containing larger units generally received priority.

From an administrative perspective, it is difficult to identify district models or approaches by which to classify rental rehab sites. In general, most programs are small (reported staffing levels in two-thirds of the sites fell below three FTEs), and most staff split their

time between the RRP and other housing and rehab programs. In terms of the allocation of functional responsibilities major variations related to the extent to which programs relied on owners to perform such tasks as collecting data on pre- and post-rehab tenants or developing the scope of work. Streamlined agencies -- those that devoted less time to assisting owners through various processing steps -- appeared to perform relatively well on most measures of program performance and to do so at considerably lower administrative costs. Administrative costs (typically covered from CDBG funds) represented about 4.4% of the per unit RRP subsidy in the typical site. For more streamlined agencies this percentage was 2%, as compared to 9% in the agencies that had adopted a handholding approach to processing and administration.

Finally, the study suggests that HUD's C/MI system -- which serves both as a funds management system and a program data base -- provides a reasonably accurate overall picture of how the program is operating. HUD is making ongoing efforts to improve the accuracy of C/MI reporting, and these charges should result in an improved data base on which future program decisions can be made.

CHAPTER 3

ROLE OF THE PHA, TENANT ASSISTANCE STRATEGIES, AND DISPLACEMENT ISSUES

Because the Rental Rehabilitation Program is part of a strategy that provides two types of subsidies -- rehab subsidies to property owners and rental subsidies for tenants -- the program typically requires two distinct organizational entities to cooperate in implementing the program. At the most basic level, rehab staff (typically part of a city housing or rehab office) and tenant assistance staff (typically PHA employees) must develop procedures and channels of communication sufficient to ensure that properties are inspected for compliance with HQS and that eligible tenants receive assistance in a timely manner. Beyond this, the program may provide an opportunity for city rehab agencies and PHAs to work more closely in implementing the RRP program in a way that meets local needs and responds to the distinct concerns of both parties.

This chapter begins with a description of the roles PHAs play in the Rental Rehab program and examines PHA perspectives on the way local programs have been designed and implemented. Section 2 of the Chapter examines the way tenant assistance resources -- both special allocations of vouchers and certificates and other local resources -- have been used in the program to date. Finally, Section 3 looks at how cities and PHAs have attempted to minimize displacement associated with the program.

3.1 Role of the PHA

As indicated previously, responsibility for Rental Rehab is most commonly located in a city or county community development agency, with day to day operations resting in a rehab office which also manages other CD funded rehab activities.¹ Within our 34-site sample, three sites -- Mesa, Arizona, St. Louis County, and San Antonio, Texas -- proved exceptional in that the Rental Rehab program was entirely PHA run. Among the remaining 31 sites, all involved a city or county rehab or program office, responsible for administering RRP grant monies, and a PHA which was responsible for administering the special allocations of certificates and/or vouchers. This section focuses on how roles and responsibilities were divided between city/county and PHA actors and the degree of cooperation and coordination achieved in the local programs to date.

3.1.1 PHA Role in Program Design

As suggested in Chapter 2, city/county administering agencies generally took the lead in developing the design for the local RRP programs. In fact, in only six (19%) of the sites did the PHA describe itself as actively involved in program design. Ten PHAs (32%) indicated that they were consulted on some aspects of the design, and 15 (or 48%) indicated no involvement in initial design decisions.

Active involvement usually included participation in early rounds of meetings and providing comments on the initial program plan. In a few cases PHA staff were asked to draft the tenant assistance

1. This study focuses on the RRP as it has been implemented by entitlement communities; state grantees are excluded from the analysis.

portion of the plan or to participate in activities such as target area selection. Consultation typically involved informal review, PHA input into the tenant assistance plan, and/or PHA input into procedures for coordinating tenant assistance with rehab activities.

While city actors were far more likely to indicate that PHAs were substantially involved or at least consulted in design decisions,¹ it is probably fair to say that most PHAs played a passive role in program design. A few PHAs indicated that there were aspects of the design that were extremely important to them, such as targeting to two bedroom units, achieving maximum lower income occupancy, and obtaining grantee approval for the interim use of Section 8 Certificates. However, once these features were incorporated, PHAs were likely to defer to city or county actors regarding the remainder of the design.

3.1.2 Definition and Evolution of Program Roles

Recognizing that the Rental Rehabilitation Program would require a cooperative effort on the part of the city's and PHAs, HUD required each grantee to execute a Memorandum of Understanding with the PHA delineating program roles and responsibilities. A review of such memoranda collected at the sample sites shows that these documents vary widely in level of detail and content. Some, for example, are extremely terse documents in which the PHA and grantee essentially agree to cooperate in the implementation of the program. In other cases, the

1. Comparable statistics provided by city respondents were 8 sites (26%) actively involved, 17 sites (55%) consulted, and only 6 sites (19%) no involvement.

memoranda are fairly extensive, providing some detail on the activities to be undertaken by each party to the agreement. Roles commonly assigned to the grantee included selecting and approving properties for the program and determining the scope of the rehabilitation work. Memoranda also frequently spelled out grantee responsibilities for obtaining data on initial tenants, pre-screening tenants, providing relocation assistance, and record keeping. PHA roles as spelled out in the memoranda typically focused on screening and processing Section 8 tenants upon notification by the grantee of project approval and completion. In addition, some memoranda specified PHA participation in conducting Housing Quality Standards (HQS) inspections or providing assistance, upon request, in determinations regarding the scope of the rehab work. Other PHA activities occasionally noted included:

- o Tenant counseling activities;
- o Record keeping for assisted households;
- o Priority processing for RRP households;
- o Providing briefing sessions on eligibility determination for program staff;
- o Providing rent reasonableness assessments in conjunction with feasibility determinations; and
- o Marketing or outreach activities.

Overall, it appears that the preparation of these memoranda was uncontroversial. Typically a draft was developed by the administering agency for review by the PHA Executive Director. In a handful of sites the PHA made minor modifications to the draft, usually to add specifics related to compliance with Section 8 regulations, but substantive issues

or problems were rare. In two sites, for example, there was some debate over which actor should be responsible for the final HQS inspection and in two others including provisions for interim use of certificates became a major PHA objective. Otherwise, the process appears to have been extremely straightforward.

Changes in PHA roles from those laid out in the Memoranda were also quite rare, with only two PHAs indicating that substantive changes had occurred. In one of these, the PHA has gone beyond the strict limits of the memorandum to provide additional guidance to the city on HQS requirements (as a result of failed inspections) and to provide more information to property owners on waiting-list and leasing requirements. In the other site, the Rental Rehabilitation Program was originally set up as a separate program, with an integrated rehab and housing assistance staff. However, after one year of operation (during which time a number of serious processing problems arose), the program was restructured to allow regular Section 8 staff to handle the housing assistance function.

3.1.3 Current Roles and Responsibilities

With a few exceptions, the roles and responsibilities undertaken by PHAs have focused on activities directly related to issuing vouchers and certificates. In five (16%) of the sites, PHA respondents indicated that they currently play a policy role in the program. In one of these sites, for example, a PHA representative sits on the project selection committee, and in several other sites, PHA staff indicated that they participate in basic program decisions as they

arise. In general, however, PHAs perceive themselves as filling a fairly narrow function related to tenant assistance.

A review of the specific activities performed by the PHAs confirms the relatively modest roles which most play in the program. For example, only four PHAs (13 percent) assisted in property selection or feasibility determination. Similarly, most PHAs are not actively involved in determinations regarding the scope of rehabilitation work required to bring RRP properties up to standard. While in nine of the sites (29%), PHA inspectors conducted a pre rehab inspection of each property (to document HQS violations and serve as input into the scope of work), program staff appeared to be generally well versed in both HQS and local rehabilitation standards, and typically performed this function without PHA assistance. In the few cases (9%) where PHA inspectors were involved in specifying needed improvements, this was typically limited to occasional consultation with rehab staff or the owner regarding specific HQS problems. Once the projects were completed, however, PHA staff played a more active role, with final inspections conducted by PHA inspectors in 80% of the sites.

While low levels of PHA involvement in property selection or rehab decisions are not particularly surprising, the nature of the PHA's involvement in many tenant related activities was somewhat more limited than might be expected. Specifically, all PHAs performed basic functions of certifying eligible households and issuing certificates and vouchers. In addition, virtually all PHAs played a role in referring new tenants to vacant RRP units. However, in only about a third of the sites did PHAs report that they were involved in such activities as

collecting data on pre- or post-rehab tenants or handling relocations. Moreover, in the vast majority of programs, PHAs indicated that they played no role in monitoring tenant turnover during the rehab stage or in verifying the accuracy of tenant data supplied to HUD.

Based on narrative descriptions of PHA and grantee activities, as well as interviewer impressions, in only a minority of the sites could the PHA be described as taking a lead role in handling tenant issues. In these sites, PHA involvement typically began at the loan approval stage, when project data (including tenant records generally obtained from the owner) were forwarded to the agency. At this point, city staff tended to drop out of the process, leaving the PHA to contact initial tenants, begin eligibility screening, and follow-up at project completion. In a few cases, these PHAs maintained intensive involvement over the construction period, making frequent contact with tenants and/or conducting occasional on-site visits.

By contrast, in the majority of sites, city actors appeared to take a "managing" role in tenant matters, with PHA activities limited to the more technical aspects of certification and processing. In a large number of cases, this interaction could best be described as "collaborative", with frequent communication between program staff and Section 8 personnel. However, in a sizable number of sites, PHA roles appeared to be essentially passive -- responding to city requests to issue certificates or vouchers to specific households. This pattern was particularly prevalent in sites where city-based staff with tenant assistance or relocation training were available. For example, in one West Coast city, a consultant was responsible for all preliminary

activities including initial tenant screening and relocation decisions as well as for coordinating with PHA staff to issue vouchers to eligible families. In another large city, a separate tenant assistance section within the administering agency managed all tenant related matters, calling on the PHA only when specific households required formal certification.

A final area of PHA involvement in the program was marketing and/or referring owners to the program. Overall, 67 percent of PHA respondents indicated that they participated in these activities, although in roughly half these cases the PHA role was limited to referring telephone inquiries to the RRP. In eleven sites (35%), however, the program made active attempts to tap current Section 8 owners through the PHA. Here, PHA staff participated by providing owner listings for general mailings, enclosing flyers or brochures in Section 8 checks, or by referring owners whose properties failed recent HQS inspections to the program. As shown in Chapter 2, sites experienced varying degrees of success in using different outreach techniques. Nevertheless, in at least a few sites, PHA referrals were considered to be the most important means of marketing the program and the source of the majority of applications.

3.1.4 PHA Satisfaction with the Program

Despite the relatively modest roles most PHAs play in the program, PHA staff are in a unique position to observe its operation and to provide independent assessments of the way grantees have implemented the RRP design. This section focuses on PHA satisfaction with various

aspects of program design and operation (see Exhibit 3.1), including the neighborhoods and projects selected for the program, tenant assistance and displacement issues, and the level of coordination achieved under the program.

Regarding the neighborhoods selected by cities for rental rehab, 68% of PHA respondents expressed general satisfaction with the types of areas in which projects were located, 10% offered no opinion, and 23% expressed dissatisfaction. Among the PHAs expressing dissatisfaction with project neighborhoods, the primary concern was that selected neighborhoods were too deteriorated for treatment under the program or were not desirable to Section 8 tenants because of lack of transportation or other amenities. This is consistent with the neighborhood ratings provided by program staff, with 65% of the units in areas characterized as "declining" also located in sites where the PHA expressed neighborhood concerns. In these sites, only 17% of the units were located in areas characterized as "improving" as compared to 50% in sites where PHAs expressed the greatest satisfaction with program neighborhoods.

Despite PHA concerns regarding project neighborhoods, reported dissatisfaction with the types of properties selected for the program or the rehab work undertaken was relatively low (6% and 13% respectively). In one site, concerns about specific properties and inadequate levels of rehab were related to the neighborhoods, which were considered to be too deteriorated for the program. The majority of rehab related concerns, however, appeared to involve relatively minor

EXHIBIT 3.1

PHA SATISFACTION WITH LOCAL PROGRAM OPERATIONS ¹

	<u>Percent Satisfied or very Satisfied</u>	<u>Percent Dissatisfied</u>	<u>Percent No Opinion</u>
Types of Neighborhoods selected for the program	68%	23%	10%
Types of properties selected	87%	6%	6%
Extent of rehab undertaken	77%	13%	10%
Rent levels post rehab	77%	16%	6%
Type of subsidy offered under the program	65%	10%	26%
Handling of tenant assistance issues	71%	10%	19%
Handling of displacement issues	68%	10%	23%
Level of PHA involvement	81%	16%	3%
Communication/coordination with rehab staff	84%	13%	3%

1. Based on 31 sites. Excludes three sites in which the PHA operated the program.

problems with HQS deficiencies necessitating reinspection by the PHA before a voucher or certificate could be issued.

With respect to post rehab rent levels, 16% of the participating PHAs expressed some concern. Several indicated that city staff led owners to believe that rents could be raised to the FMR when rent reasonableness determinations would result in lower rents. While a few PHAs suggested that they regularly approved rents as negotiated by city staffs, the majority indicated that they rigorously imposed more restrictive rent reasonableness requirements. Nevertheless, some degree of dissatisfaction with the process was evident. It is also important to note that heavy reliance on certificates (as opposed to vouchers) to date has meant that rent reasonableness determinations have operated as an upper limit in the setting of initial rents for a substantial proportion of the units.

In the area of tenant assistance and displacement issues, perhaps the most revealing statistic is the substantial level of non-response. As discussed above, in a sizable number of sites, PHA involvement in overall tenant issues was minimal. As a result, these PHAs had no basis for commenting on the extent of displacement under the program or the general handling of tenant issues. While the vast majority of PHAs appeared to be satisfied that tenant issues were properly managed, one PHA suggested that inadequate attention was being devoted to ensuring that tenants were made aware of and received assistance available through the program; this problem stemmed from a

lack of PHA staff time to monitor and follow-up with tenants.¹ In another site, the PHA expressed rather strong objections to program policies which permitted rental assistance to be offered to displacees, but not to pre-rehab tenants who merely wished to use their assistance elsewhere. Generally, such resources are made available to households living in rental rehab properties whether they are required to move or choose to move.

Not surprisingly, several of these same PHAs expressed dissatisfaction with the level of their involvement in the program (16%) and the extent of coordination between city staff and the PHA (13%). Most of these complaints revolved around city failure to provide adequate notice of when projects would be completed and lack of involvement in the project up to this time. In such cases the PHA had no way of monitoring tenant turnover during the construction period or of ensuring that the finished project would be acceptable under HQS.

While the PHA assessments reported above suggest that the administration of the program has not been completely problem free, they also indicate general satisfaction with the program and the way it is being administered by local program staff. The majority of PHAs expressed satisfaction regarding all or most aspects of program design and operation. Although the roles played by PHA staff were in some cases quite modest, in most sites, city and PHA staff appeared to be satisfied with the arrangement in place and had developed good working

1. A few PHAs also suggested that owners may empty their buildings prior to submitting a application for the RRP. While the potential for this type of abuse exists, it can not be documented and is beyond the scope of the study. However, in order to prevent such occurrences, several of our sample sites required owners to sign a statement affirming that no tenants had been evicted for a specified number of months prior to acceptance into the program.

relationships in carrying out their respective responsibilities. Principal problem areas tended to be poor communication related to the timing of project completions and HQS failures necessitating reinspection before certificates or vouchers could be issued. Both of these were mentioned in open-ended questions as well, and, overall, seven PHAs (23%) reported some problem in each of these areas.

PHAs appeared to be generally supportive of the Rental Rehab program, particularly its role in expanding opportunities for certificate holders. The most frequently mentioned strength of the program from the PHA perspective was its flexibility and the increased options for tenants who could elect to remain in the Rental Rehab properties or take their assistance elsewhere. At the same time, however, a fair number of PHAs (in many cases the same PHAs that cited increased tenant options as a program strength), felt that a weakness of the program was the fact that Section 8 assistance was not tied to the RRP units. This concern appeared to stem either from a belief that the program was not attractive enough to owners without some guarantee of future rents or a belief that the units should be "reserved" for lower income occupancy as a condition for receipt of the subsidy. Thus, while PHA staff viewed the program as a positive contribution, they did not always embrace or fully understand the split subsidy concept.

3.2 Use of Tenant Assistance Resources

As a part of the Rental Rehabilitation Program, grantees, through their PHAs, were provided with special allocations of Section 8 certificates and/or housing vouchers, in numbers roughly equivalent to one voucher or certificate per \$5,000 per Rental Rehabilitation

grant.¹ These allocations were earmarked for use in the RRP program and were to be used to minimize displacement of families living in the properties to be rehabilitated and to assist families who moved into the projects after rehab. Other resources, including regular Section 8 certificates, relocation payments, or special counseling activities might also be offered in conjunction with the Rental Rehab program.

3.2.1 Special Allocation Resources

During 1984, grantees received special allocations of both Section 8 certificates and housing vouchers, unless this would result in an extremely small voucher program. In the study sample, 25 sites received vouchers as a part of their 1984 allocations and the remainder received certificates only. In 1985 all assistance was provided in the form of vouchers. In total, the 34 sites were provided with resources sufficient to assist roughly 11,000 households, with the bulk of these resources provided in voucher form.

Actual use of these resources, however, shows a pronounced tendency to rely on the more familiar Section 8 certificates. (See Exhibit 3.2.) By mid-1986, the average site had issued approximately 8% of its total voucher allocation for use in conjunction with the Rental Rehab program, compared to about 36% of its total certificate allocation. These figures, however, mask the fact that voucher usage was concentrated in a small number of sites, with fully 20 sites having as yet issued no vouchers under the program. By contrast virtually all sites had issued certificates in conjunction with the RRP, and 13 sites

1. In future years (beginning 1987), this ratio will be reduced to 1 per \$7,500.

EXHIBIT 3.2

USE OF SPECIAL ALLOCATION RESOURCES ¹

	<u>Vouchers</u>	<u>Certificates</u>	<u>All Special Allocation Resources</u>
Mean initial allocations (1984 and 1985)	326	152	478
Percent of initial allocation issued in conjunction with the program	8.4% ²	36.1%	19.2%
Percent of resources used inside RRP projects	91.9%	83.9%	84.5%
Percent of resources used outside RRP projects	8.1%	16.1%	15.5%
Percent of initial allocation issued for interim use	1.9% ³	21.5%	9.0%
Percent of initial allocation issued for program or interim use	10.3%	57.6%	28.2%

1. Weighted to reflect the administration of the average grant dollar.

2. Actual voucher usage was concentrated in 14 sites.

3. One site reported interim use of vouchers.

Source: Usage figures supplied by PHAs, summer 1986. Figures may differ from those reported using C/MI data which contains only completed projects.

had also issued some or all of their certificates for "interim use" pending the completion of the rental rehab properties.¹ Overall, by mid-1986, the typical site had placed over half of its allocated certificates in service, but only 10% of its voucher allocation. Total special allocation resources in use by mid-1986 represented about 28% of the combined allocations in the typical site.

Several reasons accounted for the low usage of vouchers relative to certificates. Unfamiliarity with the voucher mechanism was certainly a factor. A total of six PHAs indicated that they were not yet set up to issue vouchers. Several of these noted delays associated with voucher budgets or ACCs, and at least one was still in the process of developing computer software for vouchers. It appears, however, that the majority of sites had adopted a general approach of using certificates first. Although this was usually because of greater familiarity with certificates, or because certificates were received first, several sites mentioned the five-year time limit on vouchers (beginning with first issuance) as a deterrent to use of this assistance type until needed. Another factor, mentioned in a few cases, was the higher administrative fee associated with certificates. On the whole, there did not appear to be strong resistance to the use of vouchers per se, although in a few sites generalized fears of potential "rent gouging" with vouchers (due to the absence of a rent cap) were expressed, as were complaints about the administrative hassles associated with using this new assistance type.

1. One site reporting placing vouchers in interim use.

At the time of the study, only about a third of the sites had issued both vouchers and certificates, most of these having begun by issuing certificates and, having exhausted these, moved on to vouchers. Only five sites used the two types concurrently and also indicated that there were differences in the way they used vouchers vs. certificates. In two of these sites, differences were based on unit sizes, with certificates used for two bedroom Rental Rehab units and vouchers for other unit sizes. Another site indicated that it preferred to offer vouchers to families that move from the RRP projects because the absence of a rent cap enhances the family's ability to find an acceptable unit. In addition, three of the sites indicated that project rent levels affected the type of assistance supplied. In two, vouchers were used for RRP units exceeding the FMR or for those with rents closer to the FMR. Another issued vouchers for only one project where staff expected the owner to treat the FMR as an affordability ceiling despite the absence of any cap on rents.

Overall, then, sites appeared to use their voucher and certificate allocations sequentially, usually issuing certificates first. There was little reported attempt to use the two types strategically, providing one or the other assistance type based on the characteristics of the units or households in question. While most of the PHAs did treat the Rental Rehab allocations as separate from the regular allocation at least for accounting purposes, the distinction was minimal in other sites, especially when certificates were issued for interim use. In one site, for example, Rental Rehab vacancies were

posted along with other vacant units; if a certificate holder selected the unit, that certificate became a Rental Rehab certificate.

3.2.2 Use of Other Resources

While special allocation resources constituted the primary source of assistance under the rental rehab program, regular certificates were also occasionally used. In one case, for example, all vacant RRP units had been filled by regular certificate holders, without resorting to the special allocation. In another, regular certificates were used for a few units since the special allocation certificates had been exhausted and the voucher ACC had not yet been signed. Overall, however, it did not appear that sites were in any way "supplementing" their RRP resources with additional assistance. Though a few PHAs indicated that regular certificates "might" or "could" be used in the future, given the very early stages in which the program was observed, issues related to additional or supplemental assistance needs had simply not arisen.

Use of other resources under the control of the grantees or the PHAs was also quite infrequent. For example, in one or two instances, pre-rehab tenants were able to obtain desired units in elderly Public Housing projects or other PHA controlled units, and, in one site, Public Housing units were used for the temporary relocation of a group of RRP households. Other services — such as counseling — were for the most part limited to those typically provided by the PHAs to Section 8 recipients. Similarly, grantees tended not to supplement Rental Rehab assistance with additional relocation funds. Although respondents exhibited some confusion on this point, offering contradictory

responses, it appears that grantees assumed direct responsibility for relocation costs in only a handful of the sites. In the vast majority of cases, moving and/or relocation payments were borne by owners, often as eligible expenses included in the rehab costs.

3.2.3 Assistance Levels and Strategies

As shown in Exhibit 3.2, RRP vouchers and certificates were most commonly used to assist existing tenants to remain in the Rental Rehab projects or to provide rent supplements to waiting list households who moved into the buildings. In the average site (excluding interim use) roughly 85% of the special allocation resources were used inside Rental Rehab properties, with only about 15% going to households who moved from the projects.¹

Reliance on Section 8 assistance also varied dramatically from site to site. Exhibit 3.3 shows the distribution of sites by the proportion of post rehab tenants with Section 8 assistance. In roughly half of the sites, more than 70% of all occupied units post rehab were occupied by Section 8 recipients. In 8 of these sites, the percent assisted exceeded 90%, and in 5 sites, virtually all of post rehab tenants received a certificate or housing voucher. Although most sites did not articulate an explicit strategy for the use of Section 8 resources, many had in practice operated on "one-for-one" basis.

. 1. These figures are based on data supplied by PHA staff at the time of the site visit and may include certificates issued in advance of project completion to households needing to relocate. Data presented in Chapter 4 is limited to completed projects only and shows substantially lower rates of issuance to "movers."

EXHIBIT 3.3

VARIATIONS IN ASSISTANCE LEVELS

<u>Proportion of Post Rehab Tenants With Section 8</u>	<u>Number of Sites</u>
90% - 100%	8
70% - 90%	10
50% - 70%	6
30% - 50%	6
< 30%	4

Source: HUD C/MI data.

By contrast, in 10 sites, fewer than half of all post rehab occupants were assisted. Because the program is in an early stage, site level data should be treated with caution. Nevertheless, these lower levels of assistance do appear in several cases to be consistent with attitudes expressed by the site. For example, in one site, the grantee expressed the belief that the rehab subsidy alone was sufficient to support the work and that the use of additional subsidies (in the form of rental assistance) would be "excessive." Similarly, in other sites with relatively low assistance levels, PHAs tended to play a less active role in filling vacant units, and relied on owners or tenants to seek assistance on their own, rather than actively insuring that eligible households participated in the program.

The issue of assistance levels — and the reliance different programs place on the availability of Section 8 assistance — becomes particularly important in light of proposed program changes for 1987 and beyond. Although still under review at this time, these changes call for reduced special allocations in 1987, with all special allocation resources to be directed to existing tenants, and decoupling of the tenant assistance and rehab components in 1988. The first step will preclude the "automatic" use of certificates or vouchers to fill vacant units. The second will separate the two components of the program entirely, while maintaining the availability of assistance for displaced or potentially displaced households through a system of preferences within the PHA's ongoing certificate and voucher programs.

While the impact of decoupling is beyond the scope of this study, the data do provide some insights into this matter. First, as

described above, by mid-1986 the typical site had issued less than one-third of its allocated certificates and vouchers, including resources issued for interim use. Although HUD has recently strengthened its encouragement of interim use, special allocation resources held in reserve for the RRP represent a substantial number of certificates and/or vouchers that could be put into immediate service.

Second, sites appear to vary substantially in the use of Section 8 resources, with some sites operating on a one-for-one basis and others apparently minimizing the use of Section 8 in completed units.¹ However, as was described in Chapter 2 and will be addressed again in Chapter 5, the availability of Section 8 can be an important "marketing" tool in some programs. In particular, programs operating in loose markets appear to highlight Section 8 availability in their outreach, and owners in these markets are likely to rate the availability of Section 8 as more important than the rental rehab subsidy itself. Section 8 availability may also play a role in rent controlled markets where occupancy by an assisted tenant may provide a relatively simple approach for obtaining rent increases. Thus, the impact of decoupling on program production is likely to vary by market.

1. Most sites do rely heavily on wait list tenants to fill vacant units (in fact, some PHAs insist on this). Twenty-seven PHAs either referred tenants from the waiting list to vacant lists, or in some cases provided owners with a portion of the list for the purposes of interviewing and selecting tenants. In only seven sites (21%) the PHA limited its activities to posting vacancies along with others available to Section 8 certificate holders or indicated no involvement in filling RRP vacancies. However, PHAs for the most part expected to have no ongoing role in filling vacancies, yet when asked about their expectations for the projects, 23 of 34 indicated that they thought the RRP units would be primarily occupied by assisted tenants in the future.

3.3 Anti-Displacement Strategies

The Rental Rehabilitation Program stipulates that lower income families may not be displaced without being provided financial and other assistance necessary to obtain safe, decent housing at an affordable rent. Furthermore, rental rehab grant money may not be used if rehab will result in the displacement of very low income families by families who are not very low income. Displacement occurs when a lower income family is forced to move as a direct result of rehabilitation activities. However, no household need be considered displaced if it has been offered a safe/decent and affordable unit in the project.

Vouchers and certificates constitute a primary resource available for minimizing displacement under the program, and may be used to assist eligible families to remain in rental rehab projects at the higher post-rehab rent or to assist households in moving to a new unit.¹ Other resources, such as special counseling services and relocation payments may also be offered to rental rehab tenants, but, as indicated above, these have been infrequently used, at least to date.

Grantees interviewed for this study appeared to overwhelmingly embrace the antidisplacement objective of the program, with city respondents in 28 of the sites rating "avoiding displacement" being of

1. There is some distinction between the use of vouchers and certificates for these purposes, since under the voucher program, lower (as opposed to very low) income families may only receive a voucher if they are actually forced to vacate a unit because of construction, overcrowding, or change in the use of the unit. Lower income households facing unaffordable post-rehab rents would not be considered displaced for this reason alone. Section 8 certificates, however, could be used to assist a lower income family in paying the higher rent or in finding another unit since there is no statutory requirement for actual displacement. Since all sites had available and were using certificate allocations under the rental rehab program, this would not affect displacement strategies at this point in the program.

high importance to the program. Strategies reportedly adopted by the sites for avoiding displacement included: selecting vacant properties (16 sites); selecting only projects requiring no relocation (18 sites); and selecting projects where all or most tenants are eligible for Section 8 assistance (14 sites).

When asked about the extent of displacement under the RRP, few grantees or PHAs indicated that any displacement had occurred to date. In total, eleven sites indicated that some involuntary displacement had occurred, and were able to provide information on the number of households involved or the assistance provided to them (certificates or vouchers in almost all cases). In these sites, PHA staff cited overcrowding as the principal cause of displacement, with a few additional cases resulting from relocations necessitated by physical construction or changes in unit size.

While the vast majority of PHAs and city staff indicated that there was no displacement associated with the program, it was not uncommon for one or the other respondent in each site to indicate no knowledge on this topic. The fact that in several of these cases neither city nor PHA staff could provide any information on the incidence of displacement raises what may well be one of the weak links in the Rental Rehabilitation Program: monitoring of tenant turnover during rehabilitation.

The absence of formal tenant monitoring or record keeping among the 34 sites was fairly striking. As a part of the field work for this study, interviewers attempted to identify each household that moved from a completed rental rehab project and subsequently to determine the

reason for the move and whether or not the household was assisted in its new location.¹ (These data are presented in Chapter 4.) Although information on households who had received Section 8 certificates or vouchers was readily obtainable from most PHAs, in the vast majority of cases there was no documentation on other mover households and neither PHA nor rehab staff could supply additional information. Even in cases where city or PHA staff proved to be familiar with the properties and households in question (possible only given the small size of the program to date), formal record keeping was minimal.

While the absence of records on mover households does not mean that sites are inadequately fulfilling their responsibilities with respect to tenant assistance, it does frustrate attempts to measure displacement directly. Also HUD requires local programs to maintain data on displacees, as well as tenants moving from and (initially) into RRP properties. Currently, the Department plans to provide more explicit instructions regarding these responsibilities in policy directives to grantees and HUD field offices.

In addition to recordkeeping problems, however, it was our impression that in more than a few sites, opportunities existed for potentially eligible tenants to move from the RRP projects without being thoroughly advised of their options under the program. In at least one

1. HUD CMI forms provided the starting point for this effort by identifying the number of households occupying the units pre-rehab and the number of post-rehab households who were original or "prior" tenants. Names of pre-rehab households were often available from owner applications in the project files, and occasionally other documentation, such as pre application forms for Section 8 assistance or City/PHA correspondence, was available. Information on the reason for the move and assistance status, when available, was obtained directly from program or PHA staff, or failing this, from the project owner.

case, the problem stemmed directly from misconceptions about which actor -- the grantee or the PHA -- was responsible for tenant issues. Here, city staff indicated that sole responsibility for tenant assistance and monitoring rested with the PHA, and that the city role ended with the forwarding of a tenant listing after loan approval. Conversely, PHA staff believed that their responsibilities began only with the certification of tenants for assistance, which takes place near the end of the construction period, unless notified by the city that the project involves a potential displacee. At the time of the site visit, these misconceptions were revealed, and it was also discovered that a number of pre-rehab tenants had moved from the projects entirely unbeknownst to the city.

While this represents a single case where lines of communication had clearly been confused, it suggests a need within the program as a whole to ensure that explicit responsibility for project wide tenant monitoring rests with one or the other actor. Again, HUD is in the process of addressing this issue through instructions to the field offices and changes in the Annual Performance Report (APR) requirements for grantees.

3.4 Summary and Conclusions

Overall, PHAs play a relatively modest role in the Rental Rehab program. Most PHA activities are limited to functions directly related to processing tenants for Section 8 certificates or vouchers. While some PHAs do play a "managing" role in handling overall tenant issues, in the majority of sites, city actors appear to take the lead, calling

on their PHA partners only when specific households or groups of households require certification.

PHA staff appear to be satisfied with their role in the program, and expressed general approval of the way the program has been implemented by city or county staff. Although there have been some coordination problems (most frequently related to the timing of certifications) as well as HQS problems (requiring additional minor repairs prior to unit approval), the process on the whole has run smoothly. To date, most of the assistance provided under the program has been in the form of Section 8 certificates.

The area in which the program requires the most improvement is in the documentation of displaced households and other households who have moved from the properties during the rehabilitation period. In both cases, HUD requires grantees to maintain records on basic tenant characteristics. However, data collection teams for this study found it extremely difficult to identify mover households or to determine the reasons for the move, making it impossible to measure displacement directly. In addition, it was our overall impression that sites needed to devote more attention to ensuring that tenants were informed of their options under the program and that tenant moves were monitored by one or the other of the participating actors. HUD is now in the process of clarifying tenant monitoring and data collection responsibilities in its communications to grantees and HUD field offices.



CHAPTER 4

PROGRAM IMPACT ON TENANTS

One of the key innovations of the Rental Rehab program is that it separates the subsidies to owners from the subsidies to households. While certificates and vouchers are made available to avoid the displacement of low-income families, such assistance goes to the tenant and not the project. The program's ability to serve low-income families not only depends on the extent to which such households are willing and able to occupy the units after rehab, it also depends on the extent to which market factors will keep the units well maintained and affordable over time.

Chapter 1 has already examined two important factors measuring the program's ability to serve the poor: the relationship between post-rehab rents and the FMR, and the proportion of very low-income families served in-place. While the average post-rehab unit rented for less than 90 percent of the FMR, only about 50 percent of the households served to date had lived in the project prior to rehab. Chapter 3 examined local policies towards tenant assistance and displacement. It found that, while the majority of sites were making certificates and vouchers available to RRP households, only a few communities were actively monitoring tenant mobility during rehab.

This chapter takes a closer look at the types of households that have been served by the program, including (1) households who lived in the units pre- and post-rehab ("stayers"); (2) households who occupied the units prior to rehab but moved out ("movers"); and

(3) households that moved into the RRP projects after the renovations were complete ("new residents"). The chapter begins by describing the characteristics of post-rehab tenants, distinguishing between old and new residents of RRP projects. The next section examines the affordability of the renovated units, as well as the factors that have affected the relative level of post-rehab rents. The next two sections present information on household mobility rates and the characteristics of movers and stayers, while the final section explores the reasons that households moved.

4.1 Characteristics of Post-Rehab Tenants

As described in Chapter 1, the RRP encourages the renovation of occupied buildings through one of its measures of a site's performance, namely, the proportion of very low-income tenants who had lived in the project prior to rehab. But despite this desire to serve low-income tenants in place, 25 percent of all post-rehab units were in projects that had been vacant prior to rehab. In addition, 28 percent of all pre-rehab tenants moved out of their units before the renovation was complete. As a result, post-rehab tenants represent more or less equal mix of old and new project residents (see Exhibit 4.1).

Viewed as a whole, the rental rehab program is clearly serving the types of households for which it was intended.¹ Ninety-four percent of all post-rehab tenants have incomes below 80 percent of their area-wide medians, and 79 percent are very low income households (i.e., incomes below 50 percent of the local median). New residents contain a

1. All data have been weighted to reflect outcomes achieved to date per allocated grant dollar.

EXHIBIT 4.1

DEMOGRAPHIC CHARACTERISTICS OF POST-REHAB TENANTS¹

	<u>All Post-Rehab Tenants</u>	<u>Previous Residents</u>	<u>New Residents</u>
Percent of Tenants that Lived in the Project Prior to Rehab	51.5%	N/A	N/A
Household Income			
Very Low ²	79.2%	77.7%	80.7%
Low ³	14.3	14.3	14.4
Moderate ⁴	6.5	8.1	4.9
Race/Ethnicity of Head			
White	31.0%	36.4%	25.3%
Black	53.7	52.8	54.7
Hispanic	13.4	9.1	18.1
Other	1.9	1.9	2.0
Household Type			
Elderly Households	16.9%	24.6%	9.1%
Non-elderly Households			
2-4 persons	63.7	59.2	68.2
5 or more persons	11.1	8.1	14.1
single	8.4	8.1	8.7
Sex of Head			
Female	66.7%	66.1%	67.3%
Male	33.3	33.9	32.7
Percent Female-Headed Families with Children	50.7%	40.5%	61.2%
Sample Size ⁵	956	609	347

1. Sample includes all post-rehab tenants in the 34 sites based on 6/86 CMI. Data weighted to reflect the allocation of the average grant dollar.
2. Below 50 percent of SMSA median family income as defined by HUD.
3. 50-80 percent of SMSA median family income as defined by HUD.
4. Over 80 percent of SMSA median family income as defined by HUD.
5. Sample size refers to the number of occupied post-rehab units in the 34 sites, based on 6/86 CMI. Due to missing data, the number of observations for a given variable may be lower.

somewhat higher proportion of very low income households compared to previous residents. While 6.5 percent of all post-rehab tenants have incomes above 80 percent of the SMSA median, most of these moderate income households (61 percent) were residents of the project prior to rehab.

The program was less successful, however, in its ability to serve very low income families in place. Only about 38 percent of all post-rehab tenants had incomes below 50 percent of the area median and had also lived in the project prior to rehab. As noted in Chapter 1, the lower proportion of very low tenants served in place reflects both the development of vacant units and buildings, as well as a relatively high turnover rate (28 percent) among tenants in previously occupied projects. The proportion of very low income households served in place is about 51 percent for previously occupied buildings, even though 76 percent of all post-rehab tenants in those projects have incomes below 50 percent of the local median.

Other characteristics of the post-rehab tenants are clearly in line with the program's objectives. The primary beneficiaries appear to be families; about 64 percent of all post-rehab tenants are non-elderly households with two to four members, and another 11 percent have five or more members. Seventeen percent are elderly households (of varying sizes) and the remaining 8 percent are non-elderly individuals living alone. The mix between elderly and non-elderly households differs for new and old project residents. About 26 percent of all households that had lived in the project prior to rehab have an elderly head, compared to about 9 percent for residents who are new.

The program is also serving a relatively high proportion of minorities and female-headed households with children, two subsets of the population with an above average incidence of housing needs. Two out of every three post-rehab households has a female head, and half of all households are female-headed families with children. Fifty-four percent of all post-rehab tenants are black, thirteen percent are hispanic, and two percent are other non-whites. While new and old residents are similar with respect to the sex of head, the percentage share of minorities and female-headed families with children is significantly higher among new residents.

Exhibit 4.2 presents additional information on the characteristics of "new" RRP residents, distinguishing between tenants who moved into previously occupied projects and those who moved into projects that were totally vacant prior to rehab. As is evident from the chart, the proportion of blacks among new residents of previously occupied buildings (41 percent) is considerably below the proportion black of residents of previously unoccupied projects (70 percent). Households moving into previously vacant buildings also tended to be significantly poorer, larger and younger than households in previously occupied projects, and had a higher concentration of female heads. Thus, while the rehab costs of vacant buildings tended to be relatively high (\$13,921 versus \$8,838 per unit), such properties have clearly housed the highest concentration of impoverished families.

4.2 Affordability

The program's ability to serve low-income households depends critically on the extent to which post-rehab units are affordable to the

EXHIBIT 4.2

CHARACTERISTICS OF POST-REHAB HOUSEHOLDS BY
INITIAL OCCUPANCY OF RRP PROJECT¹

	Previously Occupied Projects		Previously Unoccupied Projects
	<u>Stayers</u>	<u>Movers-in</u>	
Household Income			
Very Low Income	77.7%	72.0%	88.8%
Low Income	14.3%	21.2%	8.0%
Moderate Income	8.1%	6.7%	3.2%
Race/Ethnicity of Head			
White	36.4%	32.0%	18.3%
Black	52.8%	40.6%	70.4%
Hispanic	9.1%	25.8%	8.6%
Other	1.8%	1.6%	2.7%
Household Type			
Elderly	24.6%	15.5%	1.9%
Non-Elderly			
2-4 Persons	59.2%	59.3%	76.8%
5 or More Persons	8.1%	11.5%	18.7%
Single	8.1%	13.7%	2.6%
Sex of Head			
Female	66.1%	63.9%	74.1%
Male	33.9%	57.1%	25.9%
Percent Assisted	69.8%	64.2%	72.1%
Sample Size	609	228	194

1. Sample includes all post-rehab tenants in the 34 sites, based on 8/86 CMI. Data weighted to reflect the allocation of the average grant dollar.

poor. Exhibit 4.3 presents information on a number of relevant factors, including: (1) the level of post-rehab rents; (2) the relationship between post-rehab rents and the applicable FMR (i.e., including area-wide exception schedules);¹ and (3) the average rent increase of occupied units pre- and post-rehab.² Distributions of these variables are presented for all post-rehab tenants.

The average unit in the sample had a post-rehab rent of about \$400 per month, including utilities, or 87 percent of the applicable FMR. Twenty-nine percent of all units had rents below 80 percent of the FMR, 23 percent had rents between 81 and 90 percent, and 38 percent had rents between 91 and 100 percent of the FMR. About 10 percent of all units rented for more than the applicable FMR, but almost all of these units fell within 110 percent of that amount.

The post-rehab rents of units in previously occupied buildings were significantly higher than they had been prior to renovation, with an average rent increase of about 29 percent. However, there was a considerable amount of variance within the sample. Twenty-one percent of all units were in buildings with stable or declining rents,³ 33 percent had rent increases between one and 19 percent, 18 percent had rent increases between 20 and 39 percent, and 28 percent had rent increases of 40 percent or more.

1. FMR schedules were obtained from the local PHA.

2. HUD data do not allow a direct match of individual units pre- and post-rehab. As a result, rent increases were calculated on a project-wide basis, based on the change in the average rent of occupied units. Also, rent information on vacant units was typically missing and, when present, of questionable quality. Accordingly, the calculation is based only on occupied units.

3. Declining rents typically reflect a change in the bedroom mix of occupied units, rather than a reduction in the rent of a given unit.

EXHIBIT 4.3

THE DISTRIBUTION OF POST-REHAB RENTS¹

	<u>Distribution of Occupied Units</u>
Post-Rehab Gross Rents	
< \$300	13%
\$300 - 399	47%
\$400 - 499	21%
\$500 - 599	14%
\$600 or more	5%
	<u>100%</u>
Mean	\$399
Ratio of Rents to FMR ²	
0.80 or less	29%
0.81 - 0.90	23%
0.91 - 1.00	38%
1.01 - 1.10	9%
Over 1.10	1%
	<u>100%</u>
Mean	0.871
Average Change in Rents (%) ³	
Stable ⁴	21%
1-9 percent increase	13%
10-19 percent increase	20%
20-39 percent increase	18%
40 percent or more	28%
	<u>100%</u>
Mean	+29.0%

1. Sample includes all occupied units in the 34 sites based on 6/86 CMI. Data weighted to reflect the allocation of the average grant dollar.

2. FMR refers to applicable FMR; including area-wide exceptions.

3. Excludes units in previously vacant building.

4. Includes units in buildings where the average rent of occupied units declined.

In general, units with the largest rent increases tended to have the highest rehab costs (see Exhibit 4.4). However, neither the size of the rent increase nor the level of rehab costs were highly correlated with the level of post-rehab rents.¹ These patterns reflect the market orientation of the program. As shown in Chapter 6, variations in rehab costs are largely explained by variations in the initial conditions of RRP properties, as opposed to variations in the quality of the renovated units. Thus, while rent increases are apparently driven by the underlying increase in market values resulting from renovation, the level of post-rehab rents is unrelated to rehab costs. Such outcomes reflect the basic philosophy of the RRP program, which lets the market -- and not the government -- determine a unit's rent.

Since post-rehab rent levels are typically below the FMR, most RRP units are affordable without the provision of housing vouchers or other rental assistance for families with incomes between 50 and 80 percent of the area median. However, housing costs on the order of \$400 a month are beyond the means of most very low income households in the absence of additional assistance. As a result, two out of three post-rehab tenants are currently receiving Section 8 certificates or housing vouchers (see Exhibit 4.5). While the proportion assisted is the same for old and new residents, it varies by household income. Eighty-two percent of all very low income tenants are receiving a voucher or certificate. Only 32 percent of all households with incomes between 50 and 80 percent of

1. While the low correlation between post-rehab rents and unit rehab costs is statistically significant, it disappears altogether when one controls for bedroom size.

EXHIBIT 4.4

PEARSON CORRELATION COEFFICIENTS FOR POST-REHAB RENTS,
AVERAGE RENT INCREASE, AND PER UNIT REHAB COSTS¹

	<u>Ratio of Rents to FMR</u>	<u>Average Change in Rents (%)</u>	<u>Rehabilitation Costs per Unit</u>
Post-Rehab Rents	0.34***	0.11***	0.08***
Ratio of Rents to FMR		0.09***	-0.02
Average change in Rent (%)			0.44***

*** Statistically significant at 0.01.

1. Sample includes all occupied units in the 34 sites based on 6/86 CMI. Data weighted to reflect the allocation of the average grant dollar.

EXHIBIT 4.5

PERCENT ASSISTED BY INCOME AND PREVIOUS RESIDENCE¹

	<u>All</u>	<u>New Residents</u>	<u>Old Residents</u>
Very Low Income	82.4%	82.7%	82.2%
Low Income	31.8%	31.8%	32.2%
Moderate Income	0.0%	0.0%	0.0%
All Households	68.7%	67.7%	69.8%

1. Sample includes all occupied units in the 34 sites based on 6/86 CMI. Data weighted to reflect the allocation of the average grant dollar.

the local median are receiving some form of assistance, while none of the moderate income households are assisted. About 46 percent of all assistance being used in RRP projects is going to previous residents.

Exhibit 4.6 presents information on project rents by household income and the receipt of rental assistance. Paradoxically, moderate income households as a group had the lowest post-rehab rents, both in dollar amount and in relationship to the applicable FMR (see Column 1). They also lived in projects with the lowest proportionate rent increases. However, these differentials largely disappear when one distinguishes between assisted and unassisted households (Column 2 and Column 3). As is evident from the chart, compared to households receiving assistance, unassisted households of all income levels live in less expensive units, both absolutely and in relationship to the FMR.

This pattern may in part reflect that fact that assistance may be unnecessary when rents are relatively low. It could also reflect a tendency on the part of owners to charge higher rents to subsidized tenants (a practice known as "rent skewing"). However, the lower rents among unassisted tenants, particularly those with moderate incomes, could also be the product of household mobility. As described in more detail below, mobility rates among low and moderate income households were relatively high (34 and 41 percent, respectively) and many of these moves were related to high or greatly increasing project rents. As a result, those who remained behind would tend to be concentrated in less expensive units.

Exhibit 4.7 presents additional information on post-rehab rents, rehabilitation costs, household income, and the proportion of

EXHIBIT 4.6

PROJECT RENTS BY INCOME AND RECEIPT OF ASSISTANCE¹

	<u>Total</u>	<u>Assisted</u>	<u>Unassisted</u>
Very Low Income Households			
Average Gross Rent	\$397	\$407	\$363
Ratio of Rents-to-FMRs	0.88	0.89	0.82
Average Change in Rent ²	+29.4%	+32.2%	+18.3%
Sample Size ³	692	528	131
Low-Income Households			
Average Gross Rent	\$405	\$493	\$357
Ratio of Rents-to-FMRs	0.84	0.88	0.83
Average Change in Rent ²	+29.9%	+32.5%	+31.8%
Sample Size ³	114	23	91
Moderate Income Households			
Average Gross Rent	\$365	N/A	\$365
Ratio of Rents-to-FMRs	0.81	N/A	0.81
Average Change in Rent ²	+15.7%	N/A	+15.7%
Sample Size ³	63	0	63

1. Sample includes all occupied units in the 34 sites based on 6/86 CMI. Data weighted to reflect the allocation of the average grant dollar.

2. Excludes units in previously vacant properties.

3. Sample size for all households may exceed the sum for assisted and unassisted households due to missing data.

EXHIBIT 4.7

POST-REHAB RENTS AND TENANT INCOME BY MARKET TYPE¹

	High Rents		Low Rents	
	Low Vacancy (Tight)	High Vacancy	Low Vacancy	High Vacancy (Loose)
Average Post-Rehab Rent	\$ 491	\$ 392	\$ 327	\$ 345
Ratio of Rents-to-FMRs	0.902	0.893	0.810	0.848
Percent Below or at FMR	0.892	0.860	0.961	0.930
Average Change in Rents (%) ²	+26.9%	+20.7%	+14.1%	+37.7%
Average Rehab Costs per Unit	\$9,873	\$13,289	\$7,607	\$9,237
Percent Assisted	66.8%	64.6%	77.1%	67.9%
Household Income				
Very Low	69.3%	83.0%	84.9%	81.8%
Low	22.2%	5.4%	5.8%	15.6%
Moderate	8.4%	11.5%	9.2%	2.6%
Sample Size ³	431	188	89	288

1. Sample includes all occupied units in the 34 sites based on 6/86 CMI. Data weighted to reflect the allocation of the average grant dollar.

2. Excludes units in previously vacant properties.

3. Sample size represents the number of occupied units in each market type. Due to missing data, sample size for individual variables may be smaller.

households receiving assistance stratified by market type. In general, post-rehab rents are higher in high rent markets, both in dollar amounts and in relationship to the FMR. For example, "tight" housing markets (where rents are high in relationship to renters' incomes and vacancy rates are low) have post-rehab rents that are about 42 percent above the rents in loose housing markets (where relative rents are low and vacancy rates are high). Rehab costs are highest in high rent/high vacancy markets (\$13,287) and lowest in areas where both vacancy rates and relative rents were low (\$7,607). Despite their relatively low post-rehab rents, the largest proportionate rent increases (38 percent) were observed in low rent/high vacancy markets.

Tenant income also appears to vary with market type. Only 69 percent of all post-rehab tenants in tight housing markets have incomes below 50 percent of the area median, while about 82 percent of all tenants have very low incomes in low rent, high vacancy areas. Despite these differences in tenant incomes, the proportion of households receiving assistance is about the same in loose and tight markets. Apparently, the significantly higher rents in tighter markets necessitates gearing the program to somewhat higher income households and providing rental assistance to households with incomes between 50 and 80 percent of the area median.

Exhibit 4.8 presents the results of a simple regression equation relating the rent-to-FMR ratio in a given unit to characteristics of the tenant, the project, the owner, and the housing market. In general, the level of post-rehab rents (as measured by their relationship to the FMR) did not depend on the level of rehab costs, the

EXHIBIT 4.8
REGRESSION OF RENT-TO-FMR RATIO ON SELECTED VARIABLES

Average Rehab Costs per Unit (\$1,000s)	-0.000
Public Contribution/Rehab Costs	0.024
Previously Vacant Building (Yes=1/No=0)	-0.017
Assisted (Yes=1/No=0)	0.052***
Income of Household ¹	
Low	0.022*
Moderate	0.042***
Number of Bedrooms	-0.020***
Type of Owner ²	
Corporation	0.012
Non-Profit	0.059*
Partnership	0.027**
Cooperative	-0.091**
Other	-0.065***
Owner-Occupied Building (Yes=1/No=0)	-0.036
Previous Tenant (Yes=1/No=0)	-0.024***
Market Type ³	
High Rent/Low Vacancy (tight)	0.067***
High Rent/High Vacancy	0.114***
Low Rent/Low Vacancy	-0.035**
Constant	0.841***
R ²	0.240

*** Significant at 0.01

** Significant at 0.05

* Significant at 0.10

1. Coefficients depict differences with respect to units occupied by very low income households.

2. Coefficients depict differences with respect to units owned by individuals.

3. Coefficients depict differences with respect to units in low rent, high vacancy (loose) markets.

relative importance of the public contribution, or the initial occupancy of the building. Thus, while higher rehab costs were associated with above average rent increases, they were not associated with more expensive post-rehab units. As noted earlier, this finding attests to the market orientation of the Rental Rehab program.

Post-rehab rents did, however, vary with the receipt of rental assistance, with the rent-to-FMR ratio about 5 percentage points higher for assisted households compared to households without assistance. However, controlling for the receipt of assistance, the rent-to-FMR ratio appeared to rise with tenant income. For example, holding other factors constant, moderate income households had rent-to-FMR ratios that were about 4 percent higher than very-low income households without assistance.

The rent-to-FMR ratio also appeared to vary with type of owner and unit size. In general, smaller units had rents that were closer to the FMR. This pattern suggests that allowable rent levels have not been a significant impediment to the rehabilitation of larger units. Rent-to-FMR ratios also appeared to vary with type of owner. Ratios in buildings developed by partnerships and non-profits were 3 to 6 percentage points higher than the ratios in buildings which were owned by individuals. As described in Chapter 5, the latter control about 60 percent of the total stock. In contrast, cooperatives and "other" owners (primarily trusts) had rent-to-FMR ratios that were about 9 and 6 percentage points lower than individual owners.

Rents also appeared to vary by market type. High cost markets, regardless of their vacancy rates, had rent-to-FMR ratios between 7 and 11 percentage points higher than low rent/high vacancy areas. Since post-rehab rents are allowed to rise to their market levels, this pattern is not surprising. In contrast, rent-to-FMR ratios in low rent/low vacancy markets were about 4 percentage points below the ratios observed in low rent/high vacancy areas. This relationship is less expected, since upward pressure on rents should be less severe in markets with higher vacancies. On the other hand, somewhat higher post-rehab rents in looser markets may well be required in order to bring investors into the program.

Finally, tenants who had lived in the project prior to rehab had rent-to-FMR ratios that were about 2 percentage points lower than tenants who were new. This inverse relationship between rents and length of tenure occurs in the majority of rental markets, and reflects a reluctance on the part of property owners to increase the rents of longer term tenants, as well as a wish to avoid the relatively high costs that are associated with tenant turnover.

In general, the overall pattern of post-rehab rents is consistent with the market orientation of the Rental Rehab program. While the ratio of rents-to-the FMR varies with market conditions, it does not depend on the level of rehab costs or on the size of the rent increase. Unassisted households are generally living in the least expensive units. However, when rents are relatively high, the majority of households have Section 8 certificates or housing vouchers. The market orientation of the RRP program is seen as one of its principal

innovations. Based on our analysis, this feature of its design appears to be working.

4.3 Mobility Rates

The Rental Rehabilitation Program is clearly providing benefits to its current tenants, the majority of whom are larger families with very low incomes. However, in order to assess the program's impact on low-income households, one must also consider the households who lived in the buildings prior to rehab, but who have since moved away. If the renovation of projects has led to the displacement of initial occupants, the program's benefits to low-income households would be greatly diminished. While displacement is difficult to define and even more difficult to document, information on mobility rates does provide at least indirect evidence about its likely prevalence in the program to date.

Exhibit 4.9 presents information on the mobility rates of the tenants who occupied RRP projects prior to their renovation. The first column presents rates for all pre-rehab tenants, broken down by income, race and household type. The third column presents comparable information on the mobility rates of very low income households, who represent about 74 percent of all initial tenants. Figures in the second and fourth columns present the number of households within each category.

Twenty-eight percent of all initial tenants moved out of RRP projects during their rehabilitation. To put this statistic in some perspective, about 39 percent of all renters move in a given year in the median site within our sample. Given an average construction period of

EXHIBIT 4.9

MOBILITY RATES BY TENANT CHARACTERISTICS¹

	All Initial Households		Very Low Income Households	
	Percent Who Moved	Sample Size	Percent Who Moved	Sample Size
Income				
Very Low	20.4%	486		
Low	33.5%	91		
Moderate	41.3%	52		
Race/Ethnicity				
White	13.1%	187	9.2%	116
Black	27.1%	418	20.1%	300
Hispanic	40.6%	87	45.5%	57
Type of Household				
Elderly	16.6%	93	2.5%	77
Non-elderly				
2 to 4 persons	19.2%	462	21.4%	317
5 or more persons	33.5%	59	24.1%	41
Single	42.2%	55	20.0%	30
Sex of Head	16.6%	445	16.0%	353
Female	33.8%	247	21.9%	118
Male				
All Households	28.4%	758	20.4%	486

1. Sample includes all pre-rehab tenants in the 34 sites, based on 6/86 CMI. The data have been weighted to reflect the average outcome per allocated grant dollar. The mobility rate based on unweighted tenant data was 22 percent.

about 6 months, mobility rates within the program appear to be somewhat above mobility rates observed in the market as a whole.

In general, mobility rates in RRP projects tended to rise with household income, with moderate income households moving at almost twice the rate of households with incomes below 50 percent of the local median. Mobility rates were also relatively high among blacks and hispanics, and non-elderly individuals. At the other extreme, whites, the elderly, and female-headed households had the lowest propensity to move. Mobility patterns among very low income households by race and household type were similar to those observed in the sample as a whole, although the rates were consistently lower.

Exhibit 4.10 presents additional information on household mobility rates by certain characteristics of the projects and the units that they occupied. Mobility rates are again presented for all initial tenants and for the subset of tenants with incomes below 50 percent of the area wide median. In general, mobility rates tended to be highest in projects with the highest rent increases, the highest unit rehab costs, and the highest pre-rehab vacancy rates. Mobility rates also tended to be high in projects where average post-rehab rents were above the applicable FMR. These patterns, which were observed in the sample as a whole and for the subgroup of very low income households, suggest that a significant proportion of moves were price induced, particularly in projects involving more extensive renovation and larger rent increases.

Mobility rates also appear to vary by unit size and market type. Mobility rates are consistently lower among households in units

EXHIBIT 4.10

MOBILITY RATES BY HOUSING UNIT CHARACTERISTICS¹

	All Initial Households		Very Low Income Households	
	Percent Who Moved	Sample Size	Percent Who Moved	Sample Size
Change in Rents				
Stable or Declining	12.8%	227	6.4%	137
1-10 percent increase	19.7%	161	4.7%	96
11-40 percent increase	29.2%	186	24.9%	119
Over 40 percent increase	35.6%	184	18.4%	125
Rent-to-FMR Ratio (Post-Rehab)				
< 80 percent	22.1%	150	16.0%	109
80-89 percent	28.0%	132	17.5%	96
90-99 percent	29.9%	397	20.9%	231
100 or more	36.1%	79	32.3%	47
Per Unit Rehab Costs				
< \$5,000 per unit	17.0%	457	12.1%	289
\$5,000-\$9,999 per unit	31.0%	148	20.2%	115
\$10,000 or more	39.6%	153	31.3%	61
Number of Bedrooms				
One ²	28.8%	234	25.4%	160
Two	28.0%	393	18.0%	258
Three or more	15.0%	89	13.5%	63
Pre-Rehab Vacancy Rate				
Five percent or less	26.7%	515	18.0%	361
6-15 percent	3.6%	83	7.9%	40
Over 15 percent	36.8%	160	29.1%	87
Project Size				
One Unit	34.5%	44	12.1%	32
2-5 Units	30.8%	233	25.6%	164
6 or More Units	24.7%	481	18.1%	290
Market Type				
High Rent, Low Vacancy (Tight)	21.2%	355	17.1%	232
High Rent, High Vacancy	39.2%	151	35.7%	82
Low Rent, Low Vacancy	13.0%	58	9.6%	63
Low Rent, High Vacancy (Loose)	32.5%	194	18.7%	126

1. Sample includes all pre-rehab tenants in the 34 sites, based on 6/86 CMI. Data weighted to reflect the average outcome per allocated grant dollar.

2. This category also includes 24 efficiency apartments.

with three or more bedrooms, perhaps because of a shortage of larger units. Mobility rates are also relatively high in areas with high vacancy rates, regardless of market rent levels. Among very low income households, mobility rates in high rent, high vacancy areas are 2 to 4 times as high as they are in other markets.

In an attempt to disentangle the independent effects of these different demographic and project variables, we estimated a simple regression model predicting the probability that a household moved (see Exhibit 4.11). The dependent variable was a dummy variable with a value of one if the household moved. The independent variables included a set of measures describing the household, the project, and the housing market. Two different regressions were derived. The first was based on the sample as a whole, while the second was restricted to very low income tenants. Statistically significant relationships are signified by asterisks in the chart.

In general, mobility rates were lower for elderly and very low income households, and higher for households in projects with more extensive renovations and higher proportionate rent increases. Since, as we have seen, high rehab costs and above average rent increases tend to coincide, the combined effect of these rehab-related factors is relatively pronounced. Mobility rates among very low income households were also related to building size, with households in single-family dwellings less likely to move than households in multifamily buildings.

EXHIBIT 4.11

REGRESSIONS FOR MOBILITY RATES¹

	<u>All Tenants</u>	<u>Very Low Income</u>
Income		
Low	0.064*	N/A
Moderate	0.025	N/A
Race of Head		
Black	0.025	-0.004
Hispanic	-0.026	0.009
Other	-0.052	-0.055
Household Type		
Elderly	-0.115***	-0.162***
Large Non-Elderly (5+)	0.035	0.044
Single	0.060	-0.007
Female-Headed Households	-0.021	-0.011
Percent Change in Rents	0.153***	0.151***
Rent-to-FMR Ratio	0.189	0.175
Rehab Cost per Unit (\$1,000s)	0.020***	0.018***
2-4 Unit Building	0.075	0.120**
5 or More Unit Building	0.073	0.118*
High Vacancy/High Rent Market	-0.045	-0.046
High Vacancy/Low Rent Market	0.046	0.060
Constant	-0.268**	-0.268**
R ²	0.226	0.224

*** Significant at 0.01

** Significant at 0.05

* Significant at 0.10

1. Sample includes all pre-rehab tenants in the 34 sites, based on 6/86 CMI.

As is evident from the chart, many of the patterns that were observed in the one-way cross-tabs effectively disappear when one controls for other factors. Most notably, race and ethnicity do not appear to have an independent effect on household mobility rates. While hispanics and blacks had a higher propensity to move, this was apparently due to their concentration in projects with more extensive repairs and to their lower proportion of elderly heads. Household size, sex of head, and market type also proved insignificant. Presumably, the higher mobility rates in high vacancy/high rent areas reflect their above-average rehab costs (\$13,289 per unit), while the higher rates in high vacancy/low cost areas stem from their above average rent increases (38 percent).

4.4 A Comparison of Movers-Out and Movers-In

Another way of addressing the displacement issue is to compare the characteristics of households who moved out of RRP projects with the characteristics of those who took their place. We have seen that households who moved tended to have higher incomes than those who stayed. However, we have also seen that moves were more likely to occur in projects with higher rehab costs and larger rent increase. These data do not enable us to distinguish between voluntary moves and forced displacement. However, if movers were systematically replaced by wealthier tenants, the ability of the program to serve low-income families could well be questioned.

Accordingly, Exhibit 4.12 compares the characteristics households who moved out of RRP projects before the renovation was complete (the "movers") with the households who took their place ("new residents"). We also present information on the households who occupied the projects pre-

EXHIBIT 4.12

COMPARISON OF MOVERS AND STAYERS ¹

	<u>Stayers</u>	<u>Movers-Out</u>	<u>Movers-In</u> ²
Household Income			
Very Low Income	77.7%	61.6%	72.0%
Low Income	14.3%	20.2%	21.2%
Moderate Income	8.1%	18.2%	6.7%
Race/Ethnicity of Head			
White	36.4%	16.3%	32.0%
Black	52.8%	62.3%	40.6%
Hispanic	9.1%	19.8%	25.8%
Other	1.8%	1.5%	1.6%
Household Type			
Elderly	24.6%	15.9%	15.5%
Non-elderly			
2-4 persons	59.2%	51.1%	59.3%
5 or more persons	8.1%	14.2%	11.5%
Single	8.1%	18.8%	13.7%
Sex of Head			
Female	66.1%	44.9%	63.9%
Male	33.9%	55.1%	37.1%
Sample Size	609	167	228

1. Sample includes pre- and post-rehab tenants in the 34 sites as reported in the 8/86 CMI. Data weighted to reflect the allocation of the average grant dollar.

2. Excludes residents of previously vacant buildings.

and post-rehab (the "stayers"). To more closely focus on the displacement issue, households moving into previously unoccupied buildings have been excluded from the analysis, so that the sample of "new" tenants differs from the one described in a previous chart (Exhibit 4.1). Households moving into previously occupied buildings represent about 54 percent of all "new" post-rehab tenants.

A comparison of movers, stayers, and new tenants does not lend much support to the displacement argument. In general, households who moved out tended to be wealthier than those who stayed. They also tended to be better off than those who took their place. About 18 percent of all movers-out had moderate incomes. Only 8 and 7 percent of stayers and new residents, respectively, had incomes in this range. Movers-out and movers-in were relatively similar with respect to household type, and both had a relatively low proportion of elderly heads. However, they differed considerably with respect to race. In general, households who moved out of RRP projects had a higher concentration of blacks (62 percent) than those who stayed (53 percent) or than those who took their place (41 percent). As a result, the proportion of blacks in previously occupied projects declined after the renovation was complete.

4.5 Reasons for Moves

While mobility rates were typically higher in projects undergoing more extensive renovation and the highest rent increases, the similarities among movers-in, movers-out and stayers does not suggest the systematic displacement of low or very low income households. However, a more direct look at the displacement issue requires detailed

information on the reasons that households moved, and the assistance, if any, that they were offered in locating or renting another unit. While we attempted to get such information during our field visits, we were often unsuccessful. As described in Chapter 3, only a handful of sites attempted to monitor tenant mobility. Typically, neither the program staff nor the PHA maintained records on the names or current whereabouts of initial residents.

The information which we were able to collect is presented in Exhibit 4.13, and has been tabulated for the sample as a whole and for very low income movers. Data on the reasons for the move were missing for 59 percent of the sample households (Column 1). The fact that neither the city nor the PHA was able to provide such information is vivid testament to the general lack of monitoring that was found in the majority of sites. Typically, the treatment of tenants, particularly in the initial stages of project development, was the responsibility of project owners. Since only about half of them were interviewed, the number of unknowns is relatively large.

The two most common reasons for a move were "evictions"¹ (14.1 percent) and "voluntary moves related to rehab" (14.7 percent). The latter category includes households who moved because they were unwilling to pay higher rents; it also includes some households who, according to project owners, wished to avoid the inconveniences of renovation. Nine percent of the movers needed to relocate in order to

1. Evictions include other involuntary relocations, such as arrest.

EXHIBIT 4.13

REASONS AND OUTCOMES FOR HOUSEHOLDS THAT MOVED¹

	<u>All Households</u>	<u>Very Low Income</u>
<u>Reasons for Move</u>		
Needed to Move to Qualify for Assistance	8.9%	17.3%
Voluntary Move Related to Rehab	14.7%	4.7%
Voluntary Move Unrelated to Rehab	3.3%	3.4%
Evicted/Other Forced Relocation	14.1%	28.9%
Unknown	59.1%	45.8%
Sample Size ²	167	77
<u>Type of Assistance Offered</u>		
Vouchers/Certificates	12.4%	24.4%
Public Housing	0.1%	0.3%
Relocation Payment	0.2%	0.0%
None	60.0%	62.5%
Unknown	27.2%	12.7%
Sample Size ²	167	77
<u>Outcome for Those Offered Assistance</u>		
Refused	8.6%	9.3%
Unable to Locate Unit	5.8%	3.1%
Current Voucher/Certificate	82.3%	86.2%
Other Assistance	3.3%	1.4%
Sample Size ³	26	21

1. Data weighted to reflect the allocation of the average grant dollar.

2. Sample includes all pre-rehab tenants who moved, based on 8/86 CMI.

3. Sample restricted to movers who were offered assistance.

qualify for assistance because their units were too small, and three percent moved for a variety of personal reasons unrelated to the RRP.

As is evident from the chart, reasons for moves appear to vary with household income, although the small sample size and the extent of missing data suggest that the patterns be viewed with caution. Compared to the sample as a whole, a higher proportion of very low income households appear to have moved in order to qualify for rental assistance (17 percent), and a lower proportion moved due to other reasons related to rehab (5 percent). Very-low income households were also more prone to evictions and other involuntary relocations (e.g., arrests).

About 13 percent of all households who moved were offered some form of assistance, primarily Section 8 certificates. For very low income households, the proportion who were offered assistance was about 28 percent. This is considerably less than the proportion that would have been eligible based on income, even excluding evictions and all unrelated voluntary moves. Almost all of the households who were offered assistance accepted and received it. While the sample size is extremely small, the data suggest that about 11.5 percent of all movers, or some three percent of all initial tenants, ended up in assisted housing.

4.6 Summary and Conclusions

The Rental Rehab Program is clearly serving the population of households it was intended to serve -- seventy-nine percent of all post-rehab tenants were very low income households, and another 14 percent had incomes between 50 and 80 percent of the area median. Sixty-nine

percent were minorities and about half were female-headed families with children. Thus, households with the greatest overall incidence of housing needs appear to have been the primary recipients of program benefits.

The great majority of RRP units also meet the affordability standard adopted by HUD. While the average unit experienced a rent increase as a result of its renovation, particularly in buildings where rehab costs were high, the overwhelming majority of RRP units had post-rehab rents that were at or below the applicable FMR. The average unit in the sample rented for about 87 percent of the FMR, and only about 10 percent of all units had rents that were above the FMR. Thus, most units developed to date were affordable to low-income households (i.e., with incomes between 50 and 80 percent of the local median) even in the absence of assistance.

While post-rehab rents were modest, very low income households generally did require Section 8 certificates or housing vouchers to live in RRP units. Two-thirds of all post-rehab tenants received some form of rental assistance. About 82 percent of all very low income households were assisted, compared to only about 32 percent of all households with incomes between 50 and 80 percent of the local median. Forty-five percent of all rental assistance associated with the program went to initial occupants who remained in RRP projects, 52 percent went to residents who were new, and 3 percent went to previous residents who used their certificates or vouchers to move.

In general, the overall pattern of post-rehab rents was consistent with the market orientation of the Rental Rehab program.

While the ratio of rents-to-the-FMR varied with market conditions, it did not depend on the level of rehab costs, the size of the rent increase, or the amount of public subsidy. Such outcomes reflect the basic philosophy of the RRP program, which lets the market -- and not the local administrative agency -- determine project rents.

The program has been less successful, however, in meeting HUD's objective of serving low income households in place. Only about half of all post-rehab tenants had lived in the project prior to rehab. In part, this reflects the development of vacant properties. About 25 percent of all units were in buildings that were unoccupied at the time of rehab. However, it also reflects a relatively high rate of tenant turnover during renovation. Twenty-eight percent of all pre-rehab tenants moved out of their dwelling units before the renovation was complete.

The quality of the data do not enable us to assess the extent of displacement that has occurred to date. In general, households who moved out of RRP projects tended to have higher incomes than those who stayed or than those who took their places. While mobility rates were higher in projects with above-average rent increases, the fact that movers were replaced with lower income households tends to temper a displacement argument. Information on reasons for moves, while incomplete, also does not suggest displacement.

Nevertheless, the potential for displacement certainly exists. About 15 percent of all very low income households initially living in RRP projects moved and were apparently not offered assistance. This figure could understate the level of mobility that

actually occurred if moves were made before the project was formally accepted into the program.¹ Furthermore, many sites made little, if any, effort to contact tenants during the initial stages of renovation or to monitor household turnover. Such monitoring needs to be strengthened in order to ensure that tenants are aware of their options under the program.

1. By its nature, pre-rehab mobility would be extremely difficult to document; therefore, such data collection was not attempted as a part of this study.

CHAPTER 5

PROPERTY OWNERS AND FINANCES

The outcomes and effectiveness of the Rental Rehab Program depend to a large degree on the owners who choose to participate -- on their experience and motivations, and on the characteristics and financial condition of the units they choose to renovate. In this Chapter, we examine the characteristics of RRP owners, mechanisms for financing renovation, and the financial condition of RRP units. The Chapter begins by describing the characteristics of RRP owners and their units. Next, we explore variations in these characteristics by market and RRP subsidy type. We then turn to sources of financing for rehab expenditures, examining the share supported by public and private sources. This is followed by an analysis of the present discounted value to owners of the RRP and other contributions they receive. And finally, the Chapter concludes by exploring the extent to which rehab expenditures would have been financially feasible in the absence of RRP assistance.

5.1 Characteristics of Rental Rehab Units and Their Owners

The majority of units renovated through the Rental Rehab Program were owned by individual investors and were in small multifamily properties. As illustrated in Exhibit 5.1, about two thirds of the completed units from our 34 sample sites were in 2- to 20-unit buildings. Just over 10 percent of the completed units were in larger buildings, and about 20 percent were single-family houses. Sixty percent of the completed units were owned by individual investors, and another 17

EXHIBIT 5.1

CHARACTERISTICS OF RRP UNITS

<u>Type of Owner</u>	<u>Percentage of Units</u> ¹
Individual	60.4%
Corporation	6.2%
Partnership	17.1%
Non-profit	3.3%
Cooperative	0.3%
Other	12.8%
 <u>Size of Property</u>	
1 unit	19.5%
2-5 units	39.8%
6-20 units	28.3%
21-50 units	10.9%
51+ units	1.5%
 <u>Owner Lives in Building</u>	 6.8%
 <u>Property Completely Vacant Prior to Rehab</u>	 25.4%
 <u>Number of Bedrooms</u>	
Zero	2.9%
One	23.0%
Two	48.6%
Three or more	25.5%

1. All completed units from 34 sample sites (1,084 units), based on 6/86 CMI. Data are weighted to reflect the way in which the average allocated grant dollar has been expended.

percent by limited partnerships. Only 6 percent of the rehabbed units had corporate owners, and fewer than 5 percent were owned by non-profit organizations or cooperatives. A significant share of the completed units (about 13 percent) are listed as having "other" forms of ownership. In our sample of 125 properties, "other" owners were almost exclusively trusts.¹

Although a large share of units were owned by individual investors, relatively few (6.8 percent) were owned by resident investors. About one-fourth of completed units were in buildings that were completely vacant prior to rehab. Finally, the size distribution of units rehabbed under the RRP reflects the program's objective of expanding the supply of low-cost rental housing for families. Specifically three-fourths of the completed units had two or more bedrooms, and only three percent were efficiencies.

Exhibit 5.2 presents additional information about the owners of rental rehab units, based on our survey of 125 sample projects (with 481 units). Despite the fact that the majority of units were owned by individual investors, more than half were owned by investors whose main business is real estate and who owned other rental properties. Specifically, less than 20 percent of the Rental Rehab units were owned by investors with no other rental holdings, about 37 percent were owned by investors with between one and 15 units in other properties; and about 45 percent were owned by investors with over 15 units in other

1. Of six properties with "other" owners, five were held by trusts and one was held in joint tenancy. Property trusts are administered by banks or other trustees for the benefit of the actual owners.

EXHIBIT 5.2

ADDITIONAL OWNER CHARACTERISTICS

	<u>Percentage of Units</u> ¹
<u>Owner's Main Business is Real Estate</u>	54.3%
<u>Owner's Other Properties</u>	
None	17.4%
1-5 units	13.7%
6-15 units	23.6%
16-50 units	22.1%
51-500 units	19.9%
501+ units	3.3%
<u>Tenant Income Level in Other Properties</u>	
Low income	69.1%
Middle income	5.6%
High income	0.0%
Mixed	25.3%
<u>Year of Acquisition</u>	
Before 1970	15.5%
1970 - 1980	14.0%
1980 - 1983	19.6%
1984	26.8%
1985	20.4%
1986	3.8%
<u>Past Private Rehab Experience</u>	42.7%
<u>Past Public Rehab Experience</u>	34.5%
<u>Other RRP Properties</u>	28.6%

1. 125 sample properties (481 units), based on owner interviews. Data are weighted to reflect the allocation of the average grant dollar.

properties. Almost 70 percent of the owners with other properties indicated that their other tenants were primarily low income households.

The majority of units were acquired quite recently, and their owners were relatively inexperienced with renovating rental housing. More than half were purchased since 1983, while 20 percent were acquired in the earlier 1980s, 15 percent in the 1970s, and only 15 percent before 1970. The owners of only about 40 percent of the units had rehabbed other rental units privately, and even fewer had participated in public rehab programs. Just under one third of the completed units were owned by investors with other properties in the Rental Rehab Program.

5.2 Reasons for Participating in the Rental Rehab Program

Although most of the completed units were recently acquired, few were purchased specifically for the Rental Rehab Program. As shown in Exhibit 5.3, three quarters of completed units involved "rehab only," that is, any financing which occurred covered only the cost of repairs. About 7 percent involved the refinancing of a previously acquired property and 17 percent (labeled "purchase and rehab" in the chart) involved both acquisition and rehabilitation financing.¹

Correspondingly, surveyed owners indicated that 17 percent of completed units were "purchased specifically for the RRP." The majority of units were habitable prior to rehab, with about 40 percent requiring limited repairs and another 40 percent in more seriously dilapidated condition. Only about one in five units were judged to be uninhabitable.

1. Owners of "purchase and rehab" projects financed both the purchase of the property and its renovation as a single transaction. RRP funds, however, did not cover any of the acquisition cost; they were applied only to the cost of rehab.

EXHIBIT 5.3

TYPE OF RRP INVOLVEMENT

	<u>Percentage of Units</u>
RRP Involvement ¹	
Rehab Only	75.7%
Purchase and Rehab	17.4%
Refinancing	6.9%
Acquired for RRP ²	17.0%
Initial Condition ²	
Standard	0.7%
Limited Repairs	39.8%
Dilapidated	38.6%
Uninhabitable	20.9%

1. All completed units from 34 sample sites (1,084 units), based on 6/86 CMI. Data are weighted to reflect the allocation of the average grant dollar.

2. 125 sample properties (481 units), based on owner interviews. Data are weighted to reflect the allocation of the average grant dollar.

Most owners cited the financial incentive offered by the RRP subsidy as their primary reason for participation. Specifically, as shown in Exhibit 5.4, 40 percent of the completed units were in the program primarily because of "the attractive subsidy," another 20 percent because no other public funds were available, and 14 percent because the rehab would have been infeasible otherwise. Owners of 14 percent of the units indicated that they participated in the program primarily because they wanted to improve their properties, 10 percent cited Section 8, and 4 percent indicated a desire to benefit their low-income tenants or the surrounding neighborhood.

Focusing explicitly on financial considerations, most owners indicated that the RRP subsidy and the potential for increased cash flow from the rehabbed property were the primary incentives for participation. Specifically, when asked to identify the most important financial consideration influencing their decision to participate in the Rental Rehab Program, owners of almost two thirds of the units chose increased cash flow (from higher rents, improved occupancy rates, or lower operating costs), while about one third chose increased property values. Surprisingly, tax considerations seem to have played a relatively unimportant role — identified as the most important financial factor by owners of only 5 percent of the units. The RRP grant or loan constituted the most important form of assistance for owners of over half the completed units. But for 17 percent of the units, the Section 8 assistance was perceived as more important than the RRP subsidy, and for another 25 percent, the two forms of assistance were equally important. Thus, for owners of more than 40 percent of the

EXHIBIT 5.4

REASONS FOR RRP PARTICIPATION

<u>Main Reason</u>	<u>Percentage of Units</u> ¹
Attractive subsidy	40.2%
Otherwise infeasible	14.0%
Only public money available	18.7%
Section 8	11.7%
Improve property	13.9%
Benefit neighborhood/tenants	3.4%
Other	2.4%
 <u>Main Financial Factor</u>	
Increased cash flow	62.0%
Enhanced value	32.9%
Tax benefits	5.1%
 <u>Most Important Assistance</u>	
RRP grant or loan	57.8%
Section 8 assistance	17.3%
Equal importance	24.9%

1. 125 sample properties (481 units), based on owner interviews. Data are weighted to reflect the allocation of the average grant dollar.

units, the Section 8 subsidy was at least as important as the RRP subsidy. Apparently, these owners were more concerned about achieving full occupancy and reliable rent payments than about the capital subsidy offered by the RRP.

Different types of investors exhibited different levels of past rehab experience and different reasons for participating in the Rental Rehab Program. Exhibit 5.5 highlights the major differences by ownership form. Individual investors -- who owned about 60 percent of completed units -- were relatively inexperienced with both public and private rehab projects and were unlikely to have other properties in the Rental Rehab Program. Although almost three quarters of the individually-owned units were acquired since 1980, very few were purchased specifically for the RRP. The vast majority (90 percent) were "rehabbed only" through the program, with less than 6 percent purchased and rehabbed and only 4 percent refinanced. Individual owners tended to rehab relatively high quality units; only 14 percent of individually owned units were uninhabitable prior to rehab, and 50 percent required only limited repairs. About 60 percent of the individual owners indicated that increased cash flow constituted their primary financial motive, but almost a third placed greater emphasis on enhanced property values.

Partnerships -- accounting for 17 percent of completed units -- tended to be more experienced investors than individual owners, and a considerably larger share had other properties in the Rental Rehab Program. In addition, partnership units were more likely to have been purchased specifically for the RRP -- two-thirds of these units were acquired after 1983 and almost one-third were purchased specifically for

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EXHIBIT 5.5

TYPE OF PARTICIPATION AND MOTIVES BY OWNERSHIP TYPE

<u>Type of Involvement</u> ¹	<u>Percent of Units Owned By:</u>				
	<u>Indivs.</u>	<u>Corps.</u>	<u>Partnerships</u>	<u>Non-Profits</u>	<u>Others</u>
Rehab Only	90.3%	87.2%	65.3%	18.1%	29.9%
Purchase and Rehab	5.8%	12.8%	34.7%	81.9%	35.5%
Refinancing	3.9%	0.0%	0.0%	0.0%	34.5%
<u>Vacant Buildings</u> ¹	24.7%	19.8%	47.6%	9.6%	5.3%
<u>Initial Condition</u> ²					
Limited Repairs	49.0%	0.0%	23.8%	29.4%	39.0%
Dilapidated	36.1%	72.3%	23.3%	45.4%	61.0%
Uninhabitable	13.8%	27.7%	52.9%	25.2%	0.0%
<u>Year Acquired</u> ²					
Pre-1970	16.6%	46.3%	9.8%	0.0%	20.7%
1970s	12.1%	14.6%	21.0%	0.0%	16.5%
1980-1983	22.8%	0.0%	0.0%	41.7%	32.2%
1984-1986	48.5%	39.0%	69.3%	58.3%	30.5%
<u>Acquired for RRP</u> ²	5.4%	26.0%	32.4%	38.9%	30.5%
<u>Private Rehab Experience</u> ²	36.9%	78.1%	81.5%	16.9%	7.9%
<u>Public Rehab Experience</u> ²	28.0%	85.4%	44.8%	100.0%	7.9%
<u>Other RRP Properties</u> ²	16.6%	82.0%	38.8%	67.0%	20.7%
<u>Most Important Fin. Factor</u> ²					
Cash flow	61.1%	100.0%	63.1%	100.0%	37.3%
Value	30.2%	0.0%	36.9%	0.0%	62.8%
Taxes	8.8%	0.0%	0.0%	0.0%	0.0%
<u>Most Important Subsidy</u> ²					
RRP	57.4%	18.0%	83.9%	44.2%	38.8%
Section 8	24.9%	53.9%	3.3%	0.0%	0.0%
Equal	17.7%	28.1%	12.8%	55.8%	61.3%

1. All completed units from 34 sample sites (1,084 units), based on 6/86 CMI. Data are weighted to reflect the allocation of the average grant dollar.

2. 125 sample properties (481 units), based on owner interviews. Data are weighted to reflect the allocation of the average grant dollar.

the Rental Rehab Program. Correspondingly, over one-third of the partnership units were purchased and rehabbed through the program. Over half of the partnership units were uninhabitable prior to rehab, and, correspondingly, a relatively large share were in completely vacant buildings. Like individual investors, partnerships emphasized increased cash flow (about two-thirds) and enhanced values (about one-third) as their primary financial considerations, although surprisingly, none identified taxes as their primary financial motive for investment. Partnerships placed more weight on the RRP subsidy (as opposed to the Section 8 subsidy) than any other type of owners.

Only 6 percent of RRP units were corporate owned, but these investors were the most likely to have past experience with both public and private rehab, and over 80 percent had other properties in the Rental Rehab Program. It is interesting to note that about half the corporate owned units were acquired before 1970, but another large share -- over one-fourth -- were purchased specifically for participation in the RRP. All of the corporate owned units required substantial repairs; almost three quarters were classified as dilapidated prior to rehab, and roughly 25 percent were uninhabitable. Among corporate investors, increased cash flow was uniformly the primary financial motive; neither enhanced property values nor taxes were cited as a primary factor by these owners. This helps to explain why Section 8 subsidies were considered so much more important than the RRP subsidy by corporations; corporate investors appeared to place the highest priority on achieving and maintaining higher cash flow.

Non-profit organizations owned a very small share of RRP units (about 3 percent), but these owners probably displayed the most distinct experience and motives. All of the non-profit owners were experienced with public rehab programs and the majority had other properties in the RRP, but relatively few had any experience with private rehab investment. All of the non-profit units in our sample were purchased in the 1980s, and over half were acquired since 1983 — in many cases specifically for the Rental Rehab Program. It comes as no surprise, therefore, that most of the non-profit units (82 percent) were purchased and rehabbed through the program. Non-profit owners constituted the only group more likely to purchase and rehab units through the program than to finance rehab only. However, non-profits were no more likely than other owners to rehab the most deteriorated properties; only 25 percent of the non-profit units were uninhabitable prior to rehab, 45 percent were dilapidated, and almost a third needed only limited repairs. Non-profits focused exclusively on increased cash flow costs as their primary financial motive, and over half gave equal weight to the RRP subsidy and the Section 8 subsidy.

Finally, other types of owners (which were primarily trusts, accounting for 13 percent of RRP units) displayed the lowest level of rehab experience. About a third of their units were purchased specifically for the Rental Rehab Program, although a large share were also acquired before 1980. Units owned by other investors were roughly evenly divided between rehab only (30 percent), purchase and rehab (36 percent), and refinancing (35 percent). Thus, other investors were the only group to make significant use of the RRP for refinancing. None of

the units owned by other investors were uninhabitable prior to rehab; about one-third required limited repairs and two-thirds were dilapidated. Correspondingly, virtually none of these units were in completely vacant buildings. This group of owners placed much greater emphasis on enhanced property values than on increased cash flow. However, for 60 percent of the units held by "other" owners the Section 8 subsidy and the RRP subsidy were perceived as equally important.

Exhibit 5.6 provides a slightly different perspective on owner motivations, comparing those whose primary business is real estate to those with other occupations.¹ Not surprisingly, real estate professionals were much more experienced than other owners with both public and private rehab activities, and were more likely to have other properties in the Rental Rehab Program. Almost 60 percent of the units owned by real estate professionals were acquired after 1983, and a relatively large share were purchased specifically for the RRP. However, real estate professionals were considerably less likely than other owners to use the Rental Rehab Program as an opportunity to refinance existing properties. Not surprisingly, however, real estate professionals were more likely to take on bigger rehab jobs; almost one-third of their units were uninhabitable prior to rehab. Finally, cash flow appears to have been the primary priority for both professionals and non-professionals, although it may have been a more significant

1. The owners whose primary source of income is real estate include 20 percent of the corporate owners, 75 percent of the partnerships, 83 percent of the non-profits, 40 percent of the individual investors, and only 21 percent of "other owners."

EXHIBIT 5.6

TYPE OF PARTICIPATION AND MOTIVES BY PRIMARY BUSINESS OF OWNER

<u>Type of Involvement</u>	<u>Percent of Units¹ Owned by Entities Whose Primary Business Is:</u>	
	<u>Real Estate</u>	<u>Other</u>
Rehab Only	79.3%	68.7%
Purchase and Rehab	18.7%	18.4%
Refinancing	2.0%	12.9%
<u>Vacant Buildings</u>	35.7%	23.7%
<u>Initial Condition²</u>		
Limited Repairs	47.6	32.0
Dilapidated	21.4	59.9
Uninhabitable	31.0	13.9
<u>Year Acquired</u>		
Pre-1970	15.0%	15.9%
1970s	13.0%	14.9%
1980-1983	13.2%	25.2%
1984-1886	58.8%	44.0%
<u>Acquired for RRP</u>	21.2%	13.5%
<u>Private Rehab Experience</u>	63.2%	24.2%
<u>Public Rehab Experience</u>	44.3%	25.9%
<u>Other RRP Properties</u>	40.6%	18.8%
<u>Most Important Fin. Motive²</u>		
Cash Flow	71.4%	54.7%
Value	23.3%	40.5%
Taxes	5.3%	4.9%
<u>Most Important Subsidy²</u>		
RRP	61.1%	55.1%
Section 8	21.0%	14.2%
Equal	17.9%	30.7%

1. All completed units from 34 sample sites (1,084 units), based on 6/86 CMI. Data are weighted to reflect the allocation of the average grant dollar.

2. 125 sample properties (481 units), based on owner interviews. Data are weighted to reflect the allocation of the average grant dollar.

financial concern for professionals than for non-professional owners, who were more likely to emphasize enhanced property values as their most important financial motive for participating in the RRP.

5.3 Variations in Owner Motivations by Market Type

The benefits of the Rental Rehab Program can be expected to attract different types of owners with different motivations in different market environments. As discussed earlier, we classified our 34 sample sites on the basis of long-term rental vacancy rates and the ratio of median rent to mean renter income. Exhibit 5.7 presents owner characteristics and motivations for each of the resulting market variants. In the discussion that follows, we focus on important differences that appear to distinguish the owners in each type of market from the national average.

Loose markets are characterized by an excess supply of rental units and relatively low rent revenues. These conditions do not create a very attractive climate for investment, and are very likely to result in depressed property values. Most of the RRP units in loose markets were owned by individuals and partnerships, but about one-fourth were owned by "other" investors (primarily trusts). This is the only type of market in which the "other" owners played any significant role. Most participating property owners in loose markets appear to have used the Rental Rehab Program to achieve full occupancy and stable rent revenues in vacant or under-occupied properties, boosting short-term cash flow, but also enhancing long-term property values. More than a third of the participating units in loose markets were in vacant buildings, almost one-third were uninhabitable prior to rehab, and a third were purchased

EXHIBIT 5.7

OWNER CHARACTERISTICS, TYPE OF PARTICIPATION AND MOTIVES BY MARKET TYPE

	High Rent		Low Rent	
	Low Vacancy (tight)	High Vacancy	Low Vacancy	High Vacancy (loose)
<u>Ownership Type</u> ¹				
Individuals	61.4%	62.6%	85.2%	53.5%
Corporations	0.7%	12.2%	0.0%	9.0%
Partnerships	46.1%	13.3%	9.5%	12.3%
Non-Profits	9.7%	0.0%	1.3%	9.6%
Cooperatives	0.0%	0.0%	4.0%	0.0%
Other	4.4%	12.0%	0.0%	24.3%
<u>Real Estate Primary Business</u> ²	43.8%	60.1%	43.5%	48.2%
<u>Type of Involvement</u> ¹				
Rehab Only	83.2%	93.5%	92.6%	58.3%
Purchase and Rehab	16.8%	2.3%	5.8%	26.3%
Refinancing	0.0%	4.2%	1.6%	15.3%
<u>Vacant Buildings</u> ¹	27.1%	36.4%	25.9%	16.7%
<u>Initial Condition</u> ²				
Limited Repairs	49.9	39.6	47.2	27.5
Dilapidated	37.0	34.0	48.6	39.6
Uninhabitable	13.1	26.4	4.2	31.0
<u>Year Acquired</u> ²				
Pre-1970	15.3%	40.1%	10.6%	1.9%
1970s	16.9%	19.1%	20.2%	7.1%
1980-1983	17.9%	8.1%	8.1%	32.5%
1984-1886	50.0%	32.7%	61.1%	58.5%
<u>Acquired for RRP</u> ²	32.1%	4.0%	4.4%	13.3%
<u>Private Rehab Experience</u> ²	47.1%	66.2%	43.5%	35.0%
<u>Public Rehab Experience</u> ²				
<u>Other RRP Units</u> ²	36.1%	26.3%	31.4%	22.1%
<u>Most Important Financial Motive</u> ²				
Cash Flow	81.7%	55.8%	60.7%	46.6%
Value	15.9%	44.3%	14.1%	49.0%
Taxes	4.4%	0.0%	25.3%	4.3%
<u>Most Important Subsidy</u> ²				
RRP	65.3%	78.7%	47.5%	38.6%
Section 8	15.7%	6.6%	13.1%	26.9%
Equal	19.1%	14.7%	39.4%	34.5%

1. All completed units from 34 sample sites (1,084 units), based on CMI. Data are weighted to reflect national distribution of completed units.

2. 125 sample properties (481 units), based on owner interviews. Data are weighted to reflect national distribution of completed units.

specifically for participation in the Rental Rehab Program. Loose markets exhibited the highest incidence of both purchase and rehab and refinancing.¹

Participating owners were also relatively likely to have other properties in the RRP, suggesting that some investors in loose market environments used the program systematically as an opportunity to acquire and improve depressed properties in hopes of long-term appreciation. This hypothesis is supported by the fact that enhanced property values were just as important as increased cash flow as a motivation for participation. Moreover, investors in loose markets considered the Section 8 subsidy to be just as important as the RRP subsidy, if not more so, since Section 8 tenants offered the promise of stable rent revenues at reasonable levels.

Markets with high vacancy rates and high rents were similar to loose markets in that a fairly large proportion of the rehabbed units were in completely vacant buildings, pre-rehab property conditions were quite seriously dilapidated, and a significant share of owners were using the program to rehab multiple properties. However, almost no purchase and rehab or refinancing occurred in these markets; the Rental Rehab Program was used almost exclusively for rehab only. In part, this is a reflection of the fact that corporate investors played an unusually large role in these types of markets. Specifically, over one-fourth of the rehabbed units in these markets were owned by corporations, and, as

1. As noted earlier, "other" owners are substantially more likely than other groups to use the RRP for refinancing. Thus, it makes sense that in loose markets, where "other" owners are most evident, the incidence of RRP refinancing is high.

noted earlier, corporate owners were unlikely to use the RRP to finance both purchase and rehab, even for units purchased explicitly for the program. A very large share of the rehabbed units (60 percent) had been held by their owners for at least 15 years, suggesting that these investors saw the RRP as an opportunity to regain occupancy of vacant properties. Both increased cash flow and enhanced property values were cited as important motives for participation in the program, but -- unlike the loose market investors -- these owners did not consider the Section 8 subsidy as particularly important relative to the RRP subsidy.

Tight markets are characterized by excess demand for rental units. Landlords are unlikely to have difficulty finding tenants for their units even if the quality is poor, and property values are probably quite high. In markets of this type it is not surprising that very few vacant buildings were rehabbed, or that the availability of Section 8 assistance was relatively unimportant to investors. Half the units in tight markets needed only minor repairs prior to rehab, and less than 15 percent were classified as uninhabitable. Participating owners -- almost exclusively individuals and partnerships -- appear to have been motivated by the availability of the RRP subsidy to improve properties that they already owned in hopes of increased cash flow. Relatively few owners used the program to rehab multiple properties.

The three sites with low rents and low vacancy rates are perhaps the most difficult to interpret. These are the only markets in which cooperative owners participated in the program, although by far the majority of units were owned by individual investors. Despite the low vacancy rates, more than one-third of the units rehabbed in these

markets were in vacant buildings. However, almost none were judged to be uninhabitable. A large share were purchased recently, but not specifically for the Rental Rehab Program. In fact, only 15 percent of the participating units were purchased and rehabbed through the program, and none were refinanced. Such markets represent the only instances in which taxes were cited as the primary financial motive for participation, with owners of one-fourth of the completed units indicating that tax benefits were more important to them than cash flow or property values. Finally, the Section 8 subsidy was viewed as at least as important as the RRP subsidy by about half of the owners, just as they were in loose markets -- where rents were also low and a significant share of the rehabbed units were vacant. In other words, the availability of Section 8 assistance appears to take on the greatest significance in markets where prevailing rents are low.

5.4 Owner Motivations by Subsidy Type

The type of RRP subsidy offered by a city may influence the types of owners attracted to the program or their reasons for participating. Exhibit 5.8 presents owner characteristics and motivations for sites offering (1) grants, (2) forgivable deferred payment loans (DPLs), (3) repayable DPLs, (4) direct loans, and (5) mixed subsidies.¹ We group grants and forgivable DPLs together as non-repayable RRP contributions, while repayable DPLs and direct loans are grouped together as repayable contributions. Only two meaningful differences in owner characteristics by subsidy type emerge.

1. These subsidy types and the cities offering them are discussed in Chapter 2.

EXHIBIT 5.8

OWNER CHARACTERISTICS, TYPE OF PARTICIPATION, AND MOTIVES BY SUBSIDY TYPE

	Percent of Units in Sites Offering:				
	Grants	Forgivable DPLs	Repayable DPLs	Direct Loans	Mixed
<u>Ownership Type¹</u>					
Individuals	72.3%	74.7%	40.8%	40.3%	94.6%
Corporations	1.6%	7.8%	0.0%	17.6%	0.9%
Partnerships	5.5%	13.9%	30.8%	12.1%	4.4%
Non-Profits	20.0%	1.1%	0.0%	6.9%	0.0%
Cooperatives	0.0%	0.9%	0.0%	0.0%	0.0%
Other	0.6%	1.7%	28.4%	23.3%	0.0%
<u>Real Estate Primary Business²</u>	67.3%	52.1%	31.6%	53.0%	32.7%
<u>Type of Involvement¹</u>					
Rehab only	76.4%	86.8%	42.3%	99.3%	100.0%
Purchase and Rehab	23.6%	7.0%	42.5%	0.7%	0.0%
Refinance	0.0%	6.1%	15.2%	0.0%	0.0%
<u>Vacant Buildings¹</u>	24.8%	39.2%	28.6%	16.8%	7.0%
<u>Initial Condition</u>					
Standard	0.0%	1.8%	0.0%	0.0%	0.0%
Limited Repairs	41.7%	28.4%	37.0%	41.8%	77.9%
Dilapidated	58.3%	33.5%	48.3%	36.7%	22.1%
Uninhabitable	0.0%	36.3%	14.7%	21.5%	0.0%
<u>Year Purchased²</u>					
Pre-1970	23.0%	11.8%	0.4%	22.3%	46.2%
1970s	25.6%	15.2%	18.4%	9.0%	0.0%
1980-1983	30.2%	25.9%	20.1%	3.4%	11.5%
1984-1986	21.3%	47.1%	61.0%	65.4%	42.3%
<u>Acquired for RRP²</u>	21.8%	9.4%	34.3%	17.0%	1.4%
<u>Private Rehab Experience²</u>	54.6%	46.5%	49.8%	46.4%	5.6%
<u>Public Rehab Experience²</u>	36.7%	36.9%	48.7%	30.6%	1.4%
<u>Other RRP Units²</u>	43.0%	33.1%	19.2%	49.1%	1.4%
<u>Most Important Finance Motive²</u>					
Cash Flow	90.9%	55.9%	51.2%	45.8%	66.3%
Value	0.0%	36.3%	43.0%	24.2%	33.7%
Taxes	9.1%	7.8%	5.7%	0.0%	0.0%
<u>Most Important Subsidy²</u>					
RRP	54.6%	58.3%	62.3%	57.5%	49.7%
Section 8	9.1%	22.7%	0.0%	21.0%	37.4%
Both	36.4%	19.1%	37.7%	21.5%	12.9%

1. All completed units from 34 sample sites (1,084 units), based on 6/86 CMI. Data are weighted to reflect the allocation of the average grant dollar.

2. 125 sample properties (481 units), based on owner interviews. Data are weighted to reflect the allocation of the average grant dollar.

First, programs offering non-repayable contributions attracted a much higher share of individual owners than programs requiring repayment. Less than half the units in sites with repayable contributions were owned by individual investors. This suggests that individual owners (whether or not real estate was their primary business) were considerably less likely to participate in a program that required repayment of the RRP contribution.

Non-repayable programs also appear slightly more likely to result in the rehab of vacant buildings. The share of RRP units in completely vacant buildings was lowest for direct loan programs and highest for forgivable DPL programs. This may reflect the higher level of rehab typical of vacant buildings, which was more likely to be financially feasible when the RRP contribution was non-repayable. In fact, the share of uninhabitable units was also highest for sites offering forgivable DPLs.

It is interesting to note that the form of the RRP contribution did not have any significant impact on the importance to investors of the RRP subsidy relative to Section 8. Regardless of the type of subsidy, 50 to 60 percent of owners considered the RRP subsidy to be most important. Thus, owners who considered the Section 8 subsidy to be of equal or greater importance appear to have been influenced more by market conditions than by the depth of the RRP subsidy.

5.5 Rehab Costs and Sources of Funds

The average completed unit cost almost \$10,000 to rehab. Chapter 6 explores the relationship between rehab costs and the level and types of rehab completed. In this section, we briefly review

variations in rehab costs stemming from owner and property characteristics, and from market and subsidy characteristics. We conclude with a discussion of the relative importance of various public and private sources of rehab financing.

Exhibit 5.9 presents the average cost of rehab by owner and property characteristics, by type of involvement in the RRP, and by market and subsidy type. These data support the following initial conclusions:

- o Individual investors and "other" owners completed the least expensive rehab, while units rehabbed by partnerships and non-profits were most expensive.
- o Units that were purchased and rehabbed through the program had substantially higher costs than either units that were rehabbed only or units that were refinanced through the RRP.
- o Large properties (more than 20 units) had the lowest per unit rehab costs. In fact, the average cost for these units was roughly half of the average for all units.
- o Per unit rehab costs were over 50 percent higher in completely vacant buildings.
- o The more deteriorated the initial condition, the more costly the rehab. Units classified as uninhabitable prior to rehab were over three times more expensive than units requiring only limited repairs, and 70 percent more expensive than those in dilapidated condition.
- o Rehab costs were lower in low rent markets than in high rent markets. Moreover, among both low rent and high rent markets, rehab costs were lower in low vacancy markets than in high vacancy markets. Thus, units in low cost/low vacancy markets were least expensive.
- o Units rehabbed with direct, repayable RRP loans were about 20 percent less expensive than units rehabbed under more generous subsidy programs.

Exhibit 5.10 presents the relative importance of various sources of rehab funding for the average mean RRP unit.¹ On average,

1. Twenty percent of tax exempt loans were classified as public contributions and the remaining 80 percent were classified as private contributions.

EXHIBIT 5.9

PER UNIT COST OF REHAB

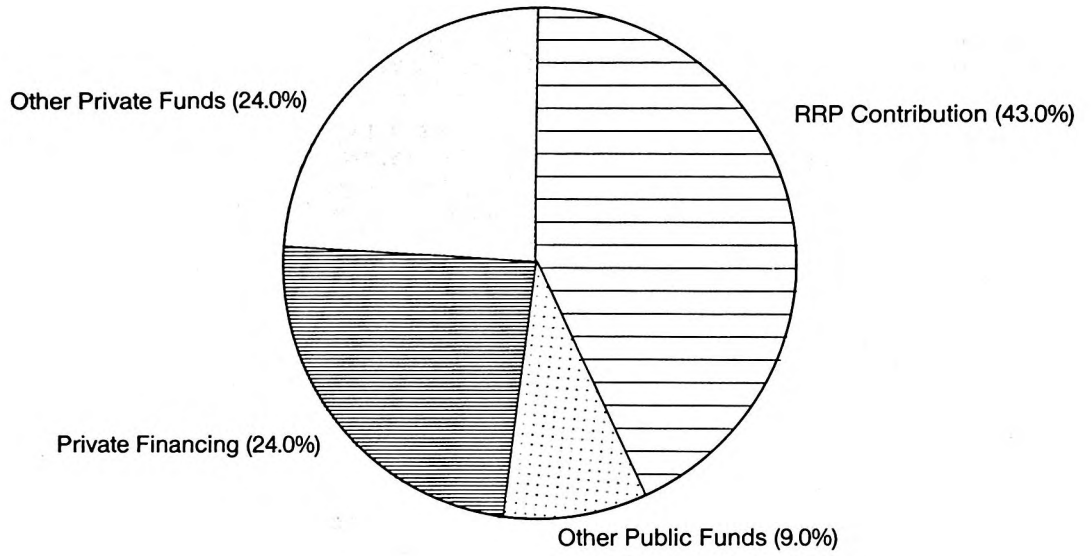
	<u>Average Per Unit Rehab Cost</u>
<u>All Units</u> ¹	\$ 9,978
<u>Ownership Type</u> ¹	
Individual	\$ 8,875
Corporation	12,676
Partnership	15,235
Non-profit	16,934
Cooperation	11,457
Other	6,406
<u>Type of Involvement</u> ¹	
Rehab Only	\$ 9,145
Purchase and rehab	15,284
Refinancing	10,983
<u>Property Size</u> ¹	
1 unit	\$12,204
2-5 units	9,973
6-20 units	11,194
21-50 units	4,668
51+ units	4,424
<u>Pre-Rehab Building</u> ¹	
Occupied	\$ 8,838
Vacant	13,921
<u>Market Type</u> ¹	
High Rent/Low Vacancy	10,314
High Rent/High Vacancy	11,950
Low Rent/Low Vacancy	7,689
Low Rent/High Vacancy	\$ 9,313
<u>Subsidy Type</u> ^{1, 3}	
Grants	\$10,273
Forgivable DPLs	11,011
Repayable DPLs	10,566
Direct Loans	7,989
Mixed	8,068
<u>Initial Condition</u> ²	
Limited Repairs	5,324
Dilapidated	10,619
Uninhabitable	17,948

1. All completed units from 34 sample sites (1,084 units), based on 6/86 CMI. Data are weighted to reflect the allocation of the average grant dollar.

2. 125 sample properties, based on owner interviews (481 units). Data are weighted to reflect the allocation of the average grant dollar.

3. Subsidy type is based on what sites offered rather than on what projects received because the CMI does not provide sufficient data in all cases.

EXHIBIT 5.10
SOURCES OF FINANCING



the cost of rehab was split evenly between public and private contributions, with public sources paying 52 percent and private sources paying 48 percent. About half the completed units received public contributions for very close to half the rehab cost (45 to 50 percent). Twenty-five percent of units received public funds totaling less than 45 percent of the rehab cost, and another 25 percent received public funding for more than half of their expenditures.

The RRP grant or loan naturally dominated the total public contribution. The RRP contribution accounted for 90 percent of public funds, with CDBG grants and loans accounting for 8 percent, tax exempt financing accounting for less than one percent, and other public contributions accounting for about 1.5 percent. For the majority of units, the Rental Rehab Program was the only source of public funds; fewer than 20 percent of units received CDBG funds, 3 percent received tax exempt financing, and 3 percent received other public contributions. However, when these additional public funds were provided, they substantially increased the total public contribution. For example, among projects that received CDBG funds, the average per unit contribution exceeded \$5,500 — 36 percent of the total cost of rehab and 43 percent of the total public contribution.

Thus, supplementary public contributions did not play a major role in the financing of the average RRP unit, but they were extremely important to the units that received them. They not only supported higher rehab costs, but they also raised the total public share substantially. To illustrate, among units receiving supplementary public funding, the average per unit rehab cost was \$14,200, 42 percent

above the average for all completed units. Moreover, the total public contribution for these units averaged 72 percent of rehab costs, compared to only 52 percent for all units.

Private contributions to the average RRP unit was evenly divided between private loan funds and other private contributions -- primarily owners' equity. However, over half of the completed units (54 percent) received no private loan funds; the private contribution came entirely from owners' equity. When private loan funds were obtained, they averaged \$6,632 per unit -- 51 percent of the total rehab cost and 93 percent of the total private contribution. The availability of private loan funds not only reduced an owner's cash contribution, it also permitted a higher per unit rehab cost. Specifically, the average rehab cost for units receiving private loan funds was \$12,070 -- 21 percent higher than the average for all units.

While most units relied heavily on owners' equity, a significant share (28 percent) required no cash contributions from their owners. In fact, the owners of 8 percent of all units actually received cash as a result of their RRP participation. In other words, the combination of public contributions and private loans exceeded the rehab cost, generating cash for the owner to "take out" of the project.¹ Among units with owners' equity contributions, the average was \$2,956 -- 36 percent of the rehab cost and 80 percent of the total private contribution. Among units that generated excess cash for the owner, the average was only \$785. Very few individual or corporate owners received

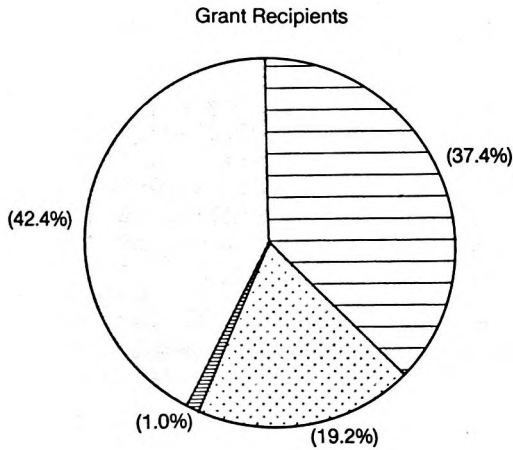
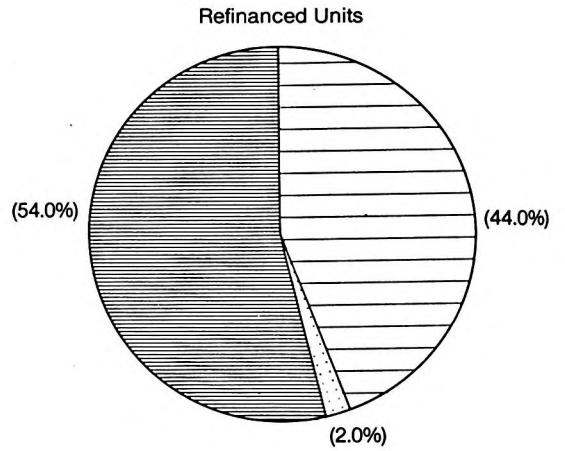
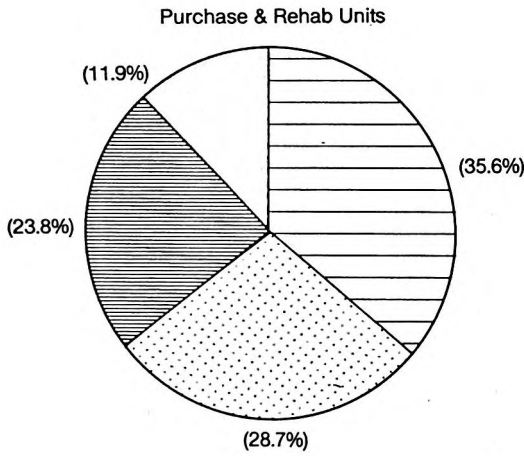
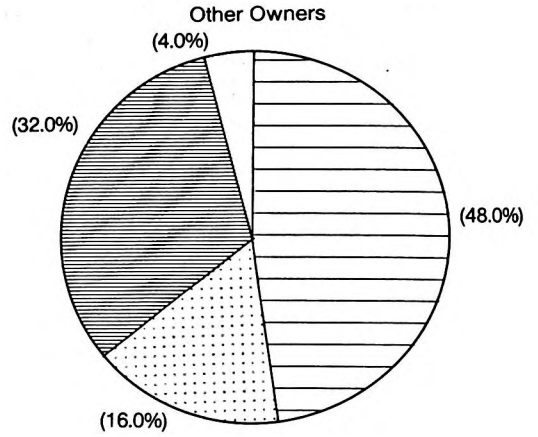
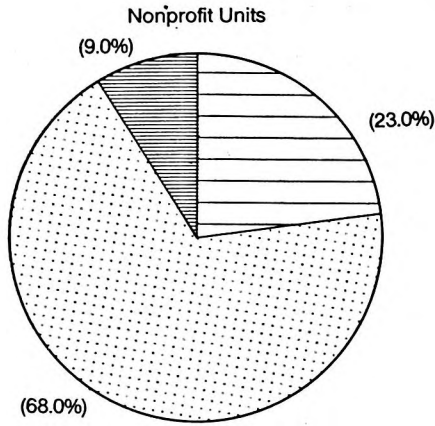
1. This calculation of excess contributions has been adjusted for owners refinancing existing debt or financing the purchase of a property.





cash through the RRP; non-profits, partnerships, and other owners were considerably more likely to do so. Surprisingly, it was not the refinanced units that generated cash for their owners, but the "rehab only" units. Finally, the highest incidence of these negative cash contributions occurred in high rent, high vacancy markets and in direct loan programs.

Owner characteristics, type of RRP involvement, and the type of subsidy all affected the relative importance of various funding sources. Exhibit 5.11 illustrates the composition of rehab financing for five particularly distinctive subsets of units:

- o Non-profit units had extremely high rehab costs. Since the average RRP contribution for these units was about the same as for all units (\$3,800), it represented a relatively small share of the total rehab cost (23 percent). The difference was made up by other public contributions, which averaged almost \$12,000 per unit — 68 percent of the total rehab cost. Private lenders contributed little to non-profit units. Not surprisingly, the non-profit owners themselves contributed even less; the average non-profit unit actually generated an excess \$165 in cash.
- o Units owned by "other" investors (primarily trusts) typically had low rehab costs. Thus, the RRP contribution (which averaged only about \$3,100) represented a fairly large share of the total (48 percent). Nevertheless, 64 percent of these units received other public contributions, so that, on average, the total public contribution exceeded 60 percent. Finally, other owners made fairly extensive use of private loan funds — accounting for almost one-third of the rehab cost on average — and therefore contributed virtually no owners' equity.
- o "Purchase and rehab" properties had relatively high per unit costs. Although the average RRP contribution to these units was high (\$4,400), it only covered 36 percent of the cost. The shortfall was covered by other public contributions, which accounted for 29 percent of total per unit costs. Altogether, the public contribution averaged almost \$9,400 per unit, or about 65 percent of the rehab cost.
- o Refinanced units made the most extensive use of private loan funds. RRP contributions covered 44 percent of the average per

EXHIBIT 5.11
VARIATIONS IN FUNDING SHARES



-  Other Private Funds
-  Private Financing
-  Other Public Funds
-  RRP Contribution

unit rehab cost, other public funds only amounted to 2 percent, and the remaining 54 percent was contributed by private lenders. Refinanced units required virtually no owner contribution, but as noted earlier, they were not used to generate cash for their owners.

- o Units receiving RRP grants were also quite likely to receive additional public contributions. The average RRP grant amounted to only 37 percent of total rehab costs but was accompanied by other public funds amounting to almost 20 percent. Thus, the total public contribution for these units averaged over \$6,700 -- 57 percent of the rehab cost. Owners of these units obtained almost no private loan funds, but provided virtually all of the remaining funds themselves.

5.6 Present Discounted Value of Public Contributions

Per unit values of public loans and grants for rental rehab are useful measures, but they do not fully capture the value of public contributions to a property owner. For example, a \$3,000 grant or forgivable DPL is clearly worth considerably more to an owner than a \$3,000 loan, and a no interest, deferred payment loan is worth more than a 5 percent self-amortizing loan for the same amount. To account for these differences, we have estimated the present discounted value to the property owner of each public contribution to rehab costs.¹ Several assumptions were made to arrive at the present discounted value estimates:

- o In the absence of the public grant or loan, the owner would have had to borrow at market terms. Most owners and lenders at the 34 sample sites indicated that rehab loans typically had interest rates of 13 percent and are amortized over 10 years.
- o The difference between annual payments at market rate and actual annual payments represents the annual benefit of the RRP and other public contributions.

1. These calculations were performed for the 125 sample properties only, because the CMI does not provide sufficient data.

- o The present discounted value of the sum of these annual benefits is estimated using an 8 percent annual discount rate.

It is important to note that the resulting present discounted value measures represent the value of public contributions to owners, not the cost to the government.

For the average (mean) completed unit, the RRP contribution was worth 40 percent of total rehab expenditures, and the total public contribution had a present discounted value to the owner of 46 percent of rehab expenditures. Exhibit 5.12 presents average benefit estimates for different types of owners and properties, both in terms of dollars per unit and as shares of total rehab costs. These results lead to somewhat different conclusions than the leveraging ratios summarized in Exhibits 5.10 and 5.11.

- o Non-profit owners contributed relatively little in private funds, but the present discounted value of the public contributions they received was actually below average. Specifically, the average value of RRP contributions to non-profit units only amounted to 33 percent of rehab expenditures, while the value of total public contributions was 43 percent.
- o Both of these ratios were considerably below the average for all units. Thus, non-profits enjoyed low leveraging ratios, but paid back the public contributions.
- o The owners receiving the most generous public subsidies appear to have been partnerships and "other" owners (trusts). In both cases, it was the supplemental public funding that made the present value of public contributions so high relative to rehab expenditures.
- o Purchase and rehab units had above average public subsidies, measured both by the conventional leveraging ratio and by the present value ratio. However, the difference in present value ratios between purchase and rehab units and other units was much smaller than the difference in conventional leveraging ratios. In other words, public contributions for these units tended to be high, but the repayment requirements were relatively stringent.

EXHIBIT 5.12

PRESENT DISCOUNTED VALUE OF PUBLIC CONTRIBUTIONS

	<u>RRP Contribution</u>		<u>Total Public Contribution</u>	
	<u>\$ Per Unit</u>	<u>Share of Rehab Cost</u>	<u>\$ Per Unit</u>	<u>Share of Rehab Cost</u>
<u>Sample Units</u> ¹	\$3,662	0.40	\$4,618	0.46
<u>Ownership Type</u>				
Individual	\$3,610	0.43	\$3,926	0.45
Corporation	4,261	0.32	5,844	0.41
Partnership	4,315	0.38	6,783	0.50
Non-Profit	3,479	0.33	4,861	0.43
Other	2,642	0.41	3,325	0.52
<u>Type of Involvement</u>				
Rehab Only	\$3,467	0.41	\$4,021	0.45
Purchase & Rehab	4,594	0.38	6,911	0.49
Refinance	4,938	0.42	4,985	0.42
<u>Property Size</u>				
1 Unit	\$4,458	0.42	\$5,031	0.45
2-5 Units	3,463	0.43	4,002	0.47
6-20 Units	2,993	0.34	4,886	0.44
21+ Units	2,347	0.42	2,347	0.42
<u>Pre-Rehab Buildings</u>				
Occupied	\$3,218	0.42	\$3,889	0.47
Vacant	4,522	0.39	5,493	0.43
<u>Initial Condition</u>				
Limited Repairs	2,523	0.43	2,721	0.46
Dilapidated	4,286	0.42	4,674	0.45
Uninhabitable	5,132	0.33	7,902	0.46
<u>Market Type</u>				
High Rent/Low Vacancy	\$3,959	0.47	\$4,734	0.51
High Rent/High Vacancy	3,038	0.44	4,091	0.51
Low Rent/Low Vacancy	5,265	0.36	6,003	0.41
Low Rent/High Vacancy	3,156	0.42	3,156	0.42
<u>Type of Subsidy</u>				
Grant	\$3,977	0.47	\$4,860	0.51
Forgivable DPL	4,924	0.54	5,506	0.57
Repayable DPL	2,810	0.26	4,195	0.32
Direct Loan	2,609	0.28	3,804	0.39

1. 125 sample properties (481 units), based on owner interviews. Data are weighted to reflect the allocation of the average grant dollar.

- o . Forgivable DPLs produced higher present value ratios than any other type of RRP subsidy. Neither grants nor forgivable DPLs required any repayment, but grants appear to have been made for smaller amounts and were accompanied by less generous supplemental contributions. Therefore, among units receiving forgivable DPLs, the RRP contribution averaged 54 percent of total rehab expenditures while the total public contribution averaged 57 percent.
- o Not surprisingly, repayable DPLs and direct loans generated the lowest benefit ratios. In fact, even though recipients of these types of subsidies often received other public contributions as well, the present value of the total public contribution was substantially below average.

In general, Exhibit 5.12 reflects surprisingly little variation in present value ratios for different types of owners and properties. The only stratifier yielding substantial systematic variation is the type of RRP subsidy. This suggests that, while the choice of subsidy type was a major determinant of the generosity of the RRP subsidy, benefits did not vary systematically along other owner and property characteristics. We tested this hypothesis by estimating regression equations that express the RRP present value ratio and the total public present value ratio as functions of owner and property characteristics, market type, and subsidy types. The results of these regressions are presented in Exhibit 5.13. They confirm that subsidy type was the primary determinant of both the RRP value ratio and the total public value ratio. Specifically, the present discounted value to an owner of the RRP contribution was highest for forgivable DPLs and grants and lowest for repayable DPLs and direct loans. The same factors, combined with the presence or absence of other public contributions, determined the present discounted value of total public contributions. The only other significant factor in these two regression equations was the dummy indicating that the market has both low vacancy rates and low costs.

EXHIBIT 5.13

DETERMINANTS OF PRESENT DISCOUNTED VALUE RATIOS

	<u>RRP Value Ratio</u>	<u>Total Public Value Ratio</u>
<u>Intercept</u>	0.346** (0.050)	0.239** (0.070)
<u>Market Types</u>		
High Vacancy/Low Rent	0.047 (0.034)	0.052 (0.034)
Low Vacancy/Low Rent	0.114** (0.045)	0.113** (0.045)
High Vacancy/High Rent	0.016 (0.040)	0.040 (0.041)
<u>Subsidy Type</u>		
Grant	0.154** (0.043)	0.155** (0.043)
Forgivable DPL	0.204** (0.033)	0.209** (0.033)
Repayable DPL	-0.060 (0.046)	-0.056 (0.047)
<u>Other Public Funds Provided</u>	—	0.290** (0.043)
<u>Pre-Rehab Condition</u>		
Dilapidated	-0.005 (0.029)	-0.005 (0.029)
Uninhabitable	-0.095** (0.042)	-0.090** (0.045)
<u>Building Vacant Pre-Rehab</u>	-0.023 (0.030)	-0.041 (0.062)
<u>Financing for Rehab Only</u>	-0.017 (0.036)	0.095 (0.062)
<u>Ownership Type</u>		
Corporation	-0.077 (0.060)	-0.093 (0.061)
Partnership	0.011 (0.037)	0.011 (0.038)
Non-Profit	-0.104 (0.014)	-0.106 (0.074)
Other	0.014 (0.066)	-0.03 (0.068)
<u>R²</u>	48.95%	55.74%

Note: ** indicates coefficients significant at the 95% confidence level.
Numbers in parentheses are standard error terms.

This suggests that in the three sites with these market characteristics, benefit levels were consistently higher than in other types of markets, although the reasons for this result are unclear.

5.7 Feasibility of Rehab in the Absence of RRP Assistance

One objective of the Rental Rehab Program is to increase the supply of standard quality rental units — to induce improvements in units that otherwise would not have been undertaken. To test the extent to which this objective has been achieved, we explore the feasibility of rehab expenditures in the absence of RRP assistance. This analysis relies on owner interviews and detailed financial data collected for our sample of 125 completed RRP properties. We begin by reviewing owner assessments of their ability to finance rehab expenditures in the absence of assistance, and then examine the financial condition of properties after the rehab investment.

Owners indicated that, even in the absence of RRP assistance, at least some of the rehab work would have been completed for almost three quarters of completed units. However, owners of only about one quarter of the units would have completed all of the rehab work required. Exhibit 5.14 summarizes owner responses to questions about the feasibility of rehab in the absence of RRP assistance. Owners of less than one fourth of the units had previously sought funding for the rehab work, and, of these, only about a third were successful.¹ Nevertheless, owners of 28 percent of the units indicated that, even without RRP assistance, they would have completed all of the rehab work,

1. We do not know why those who were successful participated in the RRP.

EXHIBIT 5.14

FEASIBILITY OF REHAB IN ABSENCE OF RRP

	<u>% of Units</u> ¹
Owner Previously Sought Financing for Current Rehab Work	22.6
Of these: % successful	34.7
Without RRP Contribution, Owner Would Have Completed:	
All of the Rehab Work	27.8
Some of the Rehab Work	43.8
None of the Rehab Work	28.4
For Those Completing Some or All of the Work:	
Estimated Expenditures/Actual Rehab Cost	0.718
Would have Completed Work All at Once	34.3
Would Have Obtained Funds from:	
Cash	46.8
Refinancing	16.0
Private Rehab Loans	15.2
Other Public Funding	5.6
Other	14.7

¹. 125 sample properties (481 units), based on owner interviews.
Data are weighted to reflect the allocation of the average grant dollar.

and 44 percent would have completed some of the work. For those who would have completed at least some of the work, the estimated rehab expenditures averaged about 60 percent of actual RRP expenditures. Moreover, only about one-third of these units would have had the work completed all at once. Thus, according to the property owners, about one-fourth of all Rental Rehab units would not otherwise have been rehabbed at all, and of the remaining three quarters, most would have been partially rehabbed, with improvements completed incrementally.¹ The primary source of financing for these improvements would have been cash.

Exhibit 5.15 highlights key variations in owner assessments of the feasibility of unassisted rehab:

- o Individual owners were the most likely to indicate that they would have undertaken the rehab work even in the absence of the RRP. On average, these owners estimated that they would have spent 82 percent of their actual rehab expenditures, but in most cases, the property improvements would have been completed incrementally.
- o Units owned by corporations and non-profits were relatively unlikely to have been rehabbed in the absence of assistance.
- o Not surprisingly, the worse a unit's condition, the less likely it was to have been rehabbed in the absence of assistance. Only about one-third of the uninhabitable units would have been rehabbed, compared to over three quarters of the units needing only limited repairs.
- o Units in loose markets (high vacancies and low rents) were much less likely to have been improved in the absence of assistance than units in any other type of market. Even among units that would have received some improvements, estimated expenditures averaged less than 60 percent of actual RRP expenditures in loose markets, and more than two-thirds of these units would have been improved incrementally rather than all at once.
- o Units receiving the most generous RRP subsidies (grants and forgivable DPLs) would have been more likely than other units

1. The result probably would not have been standard quality, at least not in the near term.

EXHIBIT 5.15

VARIATIONS IN FEASIBILITY OF REHAB

	% Completing All or Some of Work	Among Those Completing All or Some Work:	
		Mean Share Completed	% Completing Work All At Once
<u>Ownership Type</u>			
Individuals	84.1	0.82	42.5
Corporations	4.0	0.84	100.0
Partnership	63.4	0.68	23.1
Non-profit	16.8	—	23.1
Other	66.6	0.15	0.0
<u>Primary Business of Owner</u>			
Real Estate	66.1	0.78	20.8
Other	76.4	0.67	72.4
<u>Initial Condition</u>			
Limited repairs	76.8	0.71	33.2
Dilapidated	69.8	0.73	31.5
Uninhabitable	64.6	0.73	43.6
<u>Type of Market</u>			
Loose	44.6	0.59	29.7
Tight	83.2	0.73	26.6
Problem	91.0	0.70	44.6
Stable	85.0	0.91	33.3
<u>Type of Subsidy</u>			
Grants	86.8	0.88	78.5
Forgivable DPLs	79.0	0.74	30.4
Repayable DPLs	39.5	0.54	26.0
Direct Loans	61.7	0.43	15.8

1. 125 sample properties (481 units), based on owner interviews.
Data are weighted to reflect the allocation of the average grant dollar.

to be rehabbed without assistance, and a substantially larger share would have been completed all at once.¹

Another perspective on the feasibility of rehab in the absence of RRP assistance is provided by Exhibit 5.16 which presents indicators of post-rehab financial conditions -- with and without RRP assistance. Estimates of project financial conditions in the absence of RRP assistance assume that owners would have completed the same level of rehab expenditures and that they would have obtained market financing for all public contributions.² In other words, the second column of Exhibit 5.16 asks what the average unit's financial condition would have been if it had been renovated without public assistance.

For the average unit, complete renovations would not have been financially feasible without RRP assistance. In our calculations, public contributions have two major impacts: 1) they reduce the annual debt service; and 2) if they are non-repayable, they reduce the loan to value ratio. For the average unit, the annual cash flow (revenues less operating costs and debt service) would amount to less than \$200 with market financing for rehab costs, compared to about \$1,000 with RRP assistance. Almost half of all units (45 percent) would produce a negative cash flow if rehab was financed at market terms; only about one-fourth of projects would have cash flow to revenue ratios over 20 percent without RRP assistance, or cash flow to equity ratios over 10 percent. By contrast, RRP assistance produced average cash flow to

1. Note that a large share of units with generous RRP subsidies were owned by individual investors, who were very likely to indicate that they would have completed the rehab work even without assistance.

2. As discussed earlier, private lenders are assumed to provide rehab financing at 13 percent interest for a 10-year term.

EXHIBIT 5.16

IMPACT OF RRP ASSISTANCE ON PROJECT FINANCIAL CONDITIONS

<u>Average Per Unit¹</u>	<u>Rehab With RRP Assistance</u>	<u>Rehab With Market Rate Loan (No RRP Assistance)</u>
Property Value	\$31,549	\$31,549
Loan to Value Ratio	0.66	0.74
Annual Revenues	\$ 4,163	\$ 4,163
Annual Operating Costs	\$ 1,259	\$ 1,259
Annual Debt Service	\$ 1,923	\$ 2,819
Annual Cash Flow	\$ 1,054	\$, 197
Cash Flow/Revenues	0.23	0.02
Cash Flow /Equity	0.23	-0.01
<u>Cash Flow/Revenues</u>		
Less than 0	17.3%	44.7%
0-10 percent	8.4%	12.6%
10-15 percent	9.5%	14.1%
15-20 percent	8.2%	2.6%
20-30 percent	15.1%	10.9%
30-40 percent	18.5%	10.2%
40-50 percent	8.8%	8.6%
Over 50%	14.2%	3.3%
<u>Cash Flow/Equity</u>		
Less than 0	17.6%	43.0%
0-5 percent	9.6%	20.2%
5-10 percent	13.8%	13.3%
10-20 percent	22.7%	17.7%
20-30 percent	9.4%	3.0%
30-40 percent	18.1%	0.0%
Over 40%	8.8%	2.8%

1. All completed units from 34 sample sites (1,084 units), based on 6/86 CMI. Data are weighted to reflect the allocation of the average grant dollar.

revenue and cash flow to equity ratios of about 23 percent. Seventeen percent of units generated negative cash flow,¹ with 57 percent yielding cash flow to revenue ratios over 20 percent and 60 percent producing cash flow to equity ratios over 10 percent. The provision of RRP assistance does not appear to have substantially increased the share of units with very high cash flow ratios, but it did substantially reduce the share of units with very low ratios.

Exhibit 5.17 suggests several notable variations in the feasibility of unassisted rehab and in the impact of RRP assistance on project financial conditions. In the absence of RRP assistance, some types of units appear more likely than others to have been capable of supporting rehab expenditures. Specifically:

- o Units requiring only limited repairs could generate cash flow to revenue and cash flow to equity ratios of 13 percent, even with market financing.
- o Uninhabitable units would clearly be infeasible without RRP assistance, and, correspondingly units in properties that were completely vacant prior to rehab would yield lower cash flow ratios than those in occupied buildings, assuming market financing for the rehab expenditures.
- o In the absence of RRP assistance, units in low vacancy markets would yield substantially higher cash flows than units in high vacancy markets.
- o Units with RRP financing for rehab only appear more likely to have been able to support renovations in the absence of RRP assistance than purchase and rehab or refinanced units. This probably stems from the fact that purchase and rehab and refinanced units were more severely dilapidated and required costlier improvements.
- o Units with individual and "other" owners would yield relatively high cash flow ratios even in the absence of RRP assistance.

1. These are most likely to be non-profit units, although some profit motivated investors also tolerated negative cash flows, probably because of tax benefits or anticipated appreciation gains.

EXHIBIT 5.17

VARIATIONS IN FINANCIAL CONDITION

	<u>Cash Flow/Revenue</u>		<u>Cash Flow/Equity</u>	
	<u>RRP</u>	<u>Market</u>	<u>RRP</u>	<u>Market</u>
	<u>Assistance</u>	<u>Financing</u>	<u>Assistance</u>	<u>Financing</u>
<u>All Units</u> ¹	0.23	0.02	0.23	-0.01
<u>Type of Involvement</u>				
Rehab Only	0.24	0.05	0.24	0.03
Purchase and Rehab	0.20	-0.08	0.22	-0.16
Refinancing	0.12	-0.08	0.18	-0.07
<u>Ownership Type</u>				
Individual	0.23	0.05	0.28	0.05
Corporation	0.09	-0.15	0.06	-0.02
Partnership	0.25	-0.16	0.10	-0.23
Non-Profit	-0.02	-0.06	-0.09	-0.18
Other	0.25	0.10	0.31	0.03
<u>Pre-Rehab Condition</u>				
Limited Repairs	0.24	0.13	0.17	0.13
Dilapidated	0.19	-0.04	0.15	-0.12
Uninhabitable	0.25	-0.13	0.17	-0.08
<u>Building Initially</u>				
Occupied	0.22	0.04	0.25	0.03
Vacant	0.26	-0.02	0.18	-0.12
<u>Market Type</u>				
High Rent/Low Vacancy	0.25	0.10	0.09	-0.04
High Rent/High Vacancy	0.27	-0.03	0.10	0.04
Low Rent/Low Vacancy	0.23	0.07	0.10	0.06
Low Rent/High Vacancy	0.20	-0.04	0.40	0.06
<u>Subsidy Type</u>				
Grant	0.21	-0.01	0.09	0.04
Forgivable DPL	0.30	0.05	0.42	0.02
Repayable DPL	0.16	-0.06	0.16	-0.02
Direct Loan	0.14	-0.05	0.14	-0.03

1. All completed units from 34 sample sites (1,084 units), based on 6/86 CMI. Data are weighted to reflect the allocation of the average grant dollar.

- o As suggested earlier, unassisted rehab appears to have been more feasible for units that received grants and forgivable DPLs than for units with repayable subsidies.

While cash flow ratios vary quite widely when we assume market financing for rehab expenditures, the actual ratios experienced by different types of RRP units were much more constant. In other words, RRP assistance generally brought all types of units up to roughly the same level of financial health, with some notable exceptions:

- o Refinanced units, which had very high loan to value ratios, and hence, high debt service requirements, yielded below average cash flows.
- o Corporations and non-profit owners experienced low cash flows, with the average among non-profits actually less than zero. This probably resulted from the fact that the present discounted benefit ratios enjoyed by these owners were low. In other words, the RRP contributions they received must be repayed.
- o Units with repayable RRP subsidies had lower cash flows than those with grants and forgivable DPLs. Not only do these units appear to have been more dependent on RRP assistance for feasibility, but even with assistance their cash flows were low.

The evidence in Exhibit 5.17 suggests that, while most RRP units probably would not have been able to support the total rehab effort without assistance, cities have not effectively minimized subsidy benefits based on project financial conditions. In other words, the biggest benefits were not targetted to the units with the greatest financial need, and some units may have received substantially higher benefits than appear to have been needed to make rehab financially feasible. We tested this hypothesis by re-estimating the regressions presented in Exhibit 5.13 (which predict the RRP and total public present value ratios), adding the market cash flow ratio as an explanatory variable. If subsidies were effectively tailored to achieve

financial feasibility, one would expect units with the lowest market cash flow ratios (units needing the most help) to have received the biggest present value ratios. Instead, we found the coefficient on the cash flow ratio to be consistently insignificant, confirming that the size of the RRP benefit was unrelated to projects' financial needs.

5.8 Summary and Conclusions

The Rental Rehab Program has primarily attracted individual owners of smaller properties with relatively modest renovation needs. The average unit was in a building with four or five apartments and cost about \$10,000 to rehabilitate. Sixty percent of all units were owned by individuals, with partnership and trusts the next most common ownership forms (accounting for 17 and 13 percent of the sample, respectively).

While about 17 percent of all units were acquired specifically for the program, the typical investor used the RRP for the renovation of a previously held property. Fifty-eight percent of project owners indicated that the RRP grant or loan was the primary reason for their participation. However, the remaining 42 percent viewed the Section 8 subsidy as at least as important as the rehab subsidy.

Forty-three percent of the cost of the average unit was supported by the RRP grant or loan; another 9 percent was funded by other public programs; and the remaining 48 percent was covered by private funds. While only 25 percent of all units received public funding in addition to the RRP contribution, such units had substantially higher rehab costs (over \$14,000 per unit) and substantially lower leveraging ratios (each dollar of public funds was matched by less than \$0.40 in

private contributions). Private contributions were more or less evenly divided between private loans and owner's equity. When private loans were used, they were generally associated with higher rehab costs.

Since conventional leveraging ratios do not reflect the underlying value of the different subsidy types to project owners, we also calculated the net present value of the public subsidies provided by the programs. These averaged \$3,662 per unit for RRP grants and loans, and \$4,618 per unit for all public funds combined. These represent 40 and 46 percent, respectively, of the average project's rehab cost, and exhibit far less variation than conventional leveraging ratios. The net present value of forgivable DPLs (\$5,506 per unit) was about 45 percent higher than the value of repayable loans (\$3,804 per unit).

Based on survey responses of owners, three-fourths of the units would have undergone some or all of the rehab work performed under the RRP even in the absence of assistance. However, in only one-fourth of all units would the owner have completed all of the work, and in most cases, renovations on these units would have been completed incrementally rather than all at once if RRP assistance had not been provided.

Analysis of project financial conditions confirmed that complete renovations would not have been financially feasible for most units in the absence of RRP assistance. Almost half of all units would have generated negative cash flows if the total rehab effort had been supported with private financing, and two-thirds would have had cash flow to revenue ratios under 10 percent. Nevertheless, subsidy levels

were not effectively tailored to project financial conditions, and in many cases, cities provided larger subsidies than the minimum required to make rehab financially feasible. While greater use of gap financing techniques could have helped to minimize subsidies, sites evidently viewed this as a trade-off, preferring a straight 50 percent-of-cost approach that was both attractive to potential participants and easy to administer.



CHAPTER 6

PROPERTY CONDITIONS AND REPAIRS

The Rental Rehabilitation Program provides substantial discretion to localities with respect to the condition of assisted buildings prior to rehabilitation and the type and extent of repairs. Program regulations require that, prior to rehab, assisted projects fail at least one condition related to state or local housing code or Section 8 Housing Quality Standards (HQS). They also establish a minimum rehab cost of \$600 per unit and a maximum RRP grant of \$5,000 per unit (allowing for some adjustments in high cost areas). However, within these broad constraints, cities can participate in the funding of a variety of rehabilitation projects, ranging from light renovation to major structural work. Localities are responsible for defining the "essential improvements" over and above code/HQS that are eligible for program funding.

This chapter examines the level and extent of renovation that has been funded under the program. It begins by describing the initial conditions of RRP projects, as well as the specific types of repairs that have been made. It then examines both the quality and the scope of the work that was done, and presents a detailed breakdown of rehab costs by type of system replaced or repaired, and by whether the expenditures were required to meet local codes and/or HQS. Finally, it presents the results of a regression equation examining the independent effects of a number of different factors influencing rehab costs.

The analysis is based on a sample of 125 projects with 492 units distributed more or less evenly across the sites.¹ These projects represent about 45 percent of all projects and units that have been completed in the 34 sites. As part of the on-site data collection effort, project team members with a background in housing inspection or code enforcement examined work write-ups and other documents contained in program files, interviewed city rehab specialists and project owners, and conducted on-site inspections of the sampled properties.² These efforts produced a detailed account of the nature, quality, and costs of repairs that have been supported under the program to date.

Before turning to these findings, it is important to understand both the flexibility which the program provides to local grantees in determining eligible repairs, and the methods used in this evaluation to classify these repairs. The RRP is constrained by the requirements that post-rehab units must satisfy the local housing code and Section 8 Housing Quality Standards (HQS), the latter being a set of service standards applicable to the certificate and voucher programs. Nevertheless, the program allows localities and owners the flexibility to jointly specify RRP-subsidized rehab work that goes beyond local code and HQS when this work seems essential for sound management or marketability. Localities sometimes also allow owners to make general property improvements that are not essential to sound management and

1. See Appendix A for a detailed description of the sampling methodology.

2. Not all units in sampled projects necessarily were inspected, but this is valid since the property is the basic unit of analysis.

marketability, and sometimes even count owner expenditures on these improvements as part of the owner's match for RRP funds.

The local flexibility inherent in the RRP has been controversial. Some people feared that RRP would fund improvements that were excessive for moderate income housing. Others felt that owners and local program staff were in the best position to know what was appropriate for individual units. To address the variations in repairs that resulted from local flexibility, data were collected on how much was spent on each of three types of repairs (repairs required to meet code or HQS, other essential repairs, and general property improvements), as well as the nature of these expenditures. However, simply recording the expenditures allocated to these classes locally, ran the risk that the data would coningle the effects of "name choice" with actual variations in the rehab allowed. For example, if a locality largely ignored these distinctions and simply identified all work as related to local code or HQS, data on expenditures by category provided by the city would not reveal if any funds were spent on luxury-class items. Therefore, in addition to collecting data on expenditures as classified by the city, this evaluation examined the individual work write-ups and reclassified some expenditures based on uniform decision rules. While these decision rules do not reflect local standards, they provide a uniform description of the rehab performed from a national perspective. The classification system and the extent of reclassification are discussed further in Section 6.3 and Appendix C.

Use of an independent classification creates a potential weakness in the data, one that also is inherent in the assessments

reported in this chapter of the quality of workmanship and materials involved in the rehab and of whether residual improvements were needed post-rehab. The data are simply the independent judgments of the inspectors on the project team. Although a two-day training session was used to increase the uniformity and appropriateness of their judgments, and all work was reviewed centrally for accuracy and consistency, some residual variation undoubtedly exists among the inspectors. More importantly, the deviation of local judgments from the uniform decision rules used in this evaluation does not necessarily imply a local program deficiency.

6.1 Pre-rehab Conditions and Nature of Repairs

Information on the initial conditions of RRP projects was obtained by reviewing project work write-ups and inspection reports, and by classifying each of 17 different building systems (listed in Appendix C) as: (1) "sound," (2) having "minor deficiencies," (3) having "incipient code violation or HQS failure," or (4) having a "major deficiency." Based on this detailed assessment, as well as on subsequent interviews with program staff and project owners, each sampled project was placed into one of four general categories: (1) sound and met all local standards; (2) in need of limited repairs; (3) dilapidated;¹ and (4) uninhabitable.

As shown in Exhibit 6.1, less than one percent of the sampled units (consisting of three units in one property) were in sound condition prior to rehab.² About 40 percent of all units were in need

1. Defined as requiring more than limited repair but not uninhabitable.

2. The only major repair that occurred in this property was the replacement of an antiquated heating system.

EXHIBIT 6.1

PRE-REHAB CONDITIONS OF PROPERTIES

<u>Condition</u>	<u>Distribution of Properties</u>	<u>Distribution of Units</u>
Sound	0.7%	0.7%
In Need of Limited Repair	39.3	39.8
Dilapidated	39.4	38.6
Uninhabitable	<u>20.6</u>	<u>20.9</u>
	100.0%	100.0%

Note: Based on discussion with owners and local rehab specialists and a review of work write-ups for the 125 sampled properties. Results are weighted to population estimates. See text for further definition of conditions.

of limited repairs, 39 percent were dilapidated, and 21 percent were uninhabitable. The rental rehab program was designed to serve properties requiring only a moderate level of repairs. Based on our analysis, about 79 percent of all sampled units would appear to fall in this range.

Exhibit 6.2 presents information on the frequency of major systems replacements or repairs by the initial condition of the project and for the sample as a whole. The average unit had major work performed on 3.4 different systems. Over half of all units had their electrical systems and bathrooms replaced, while only about a quarter of all units had major structural repairs. Not surprisingly, the frequency of repairs within each category rises as the initial condition of the property declines. The average number of systems that were replaced or repaired is also inversely related to the initial quality of the project.

On average, units that were in need of limited repairs had two of the eight major systems listed in Exhibit 6.2 overhauled or replaced. As shown in column one, about one-third of all units in this category had major repairs to their roofs or to their electrical or heating systems. About one-quarter had their kitchens or bathrooms replaced, and about one-fifth had their windows replaced or their plumbing systems overhauled. Major structural work was almost never undertaken, and the few exceptions involved adding or reconfiguring units.

The number of major systems replaced or repaired increased dramatically for dilapidated projects, which had work performed on an

EXHIBIT 6.2

FREQUENCY OF MAJOR SYSTEM REPAIR OR REPLACEMENT
BY PRE-REHAB CONDITION

<u>System</u>	<u>In Need of Limited Repairs</u>	<u>Dilapidated</u>	<u>Uninhabitable</u>	<u>All Units</u>
Roof	33%	41%	67%	40%
Heating	34%	52%	80%	48%
Plumbing	19%	53%	65%	40%
Electrical	34%	73%	90%	61%
Windows	17%	27%	60%	31%
Structural	3%	38%	59%	27%
Kitchen	26%	52%	75%	44%
Bathrooms	22%	63%	83%	50%
Number of Systems with Major Work	1.9	5.0	6.0	3.4

Note: Based on discussion with owners and local rehab specialists and a review of work write-ups for the 125 sampled properties. Results are weighted by the number of units in each project. For unit-specific items, data were collected on the percentage of units in the project that were in each condition.

average of five major systems. Seventy-three percent of all units had major electrical work, and 63 percent had their bathrooms replaced. About half of all sampled units had their kitchens overhauled or their heating or plumbing systems replaced or repaired. Structural repairs were much more common among dilapidated units compared to units in need of limited repairs (38 versus 3 percent). While the frequency of roof repair was also somewhat higher in dilapidated units, the difference was relatively small, probably because such work becomes both difficult and costly to delay once a roof deteriorates beyond a certain point.

Uninhabitable projects had an average of six major systems overhauled or replaced. Major systems work in these properties was spread across all systems, with the least frequent, complete window replacement and major structural work, performed in 60 percent of all units. Electrical and heating systems were overhauled in virtually all of the uninhabitable properties, and the great majority of units had their kitchens and bathrooms replaced.

While not shown in the chart, we estimate that about 17 percent of all projects rehabilitated with program funds include either added bedrooms in selected units or newly created units. The program's emphasis on larger units seems to have stimulated many of these reconfiguration efforts.

6.2 Quality and Scope of Repairs

The overall quality of the rehabilitation which has been supported under the program was measured by rating project repairs according to two broadly defined criteria: (1) the quality of the work that was actually done (based on materials and execution); and (2) the

completeness of the scope of work. The latter involved categorizing the condition of projects after rehab as "complete," "minor repairs still needed," or "major repairs/replacements required." The results of these assessments are presented in Exhibit 6.3.

According to our estimates, 71 percent of all sampled units had repair work that was rated as involving "average" workmanship and materials, and another 20 percent received a "high" quality rating. Only about 9 percent of the sampled units had repairs that our staff rated as "poor" workmanship or materials. Thus, in this respect, the RRP has been successful in producing quality work.

However, at the time of our site visits, our inspectors felt 34 percent of the sampled units would have benefitted from further work appropriate to modest income housing. In 25 percent of these units, code and HQS requirements were met, but in the opinion of our inspectors, additional minor repairs would have improved the project's marketability or operating efficiency. Clearly, the existence of these residual needs was a judgmental issue. Some of the desirable repairs also might not have been supportable given the property's existing debt load and expense profile. Furthermore, in a few units, the repair needs appeared to result from tenant abuse after rehab.

Less judgmental was the finding that nine percent of the units had major deficiencies at the time of our site visits. These units should fail a code or Section 8 housing quality inspection. For the most part, these were the same units which received a poor quality rating on the work that was done. Overall, about 9 percent of the total

EXHIBIT 6.3

DISTRIBUTION OF UNITS BY QUALITY AND SCOPE OF REPAIRS

	<u>All Units</u>	<u>Quality of Workmanship and Materials</u>		
		<u>Above Average</u>	<u>Average</u>	<u>Below Average</u>
All Units	100%	19.6%	71.3%	9.1%
Items in Scope of Work				
Complete	65.6%	86.5%	68.2%	0.0%
Minor Repairs Still Desirable	25.1%	12.0%	30.3%	13.0%
Major Repairs Required	<u>9.3%</u>	<u>1.5%</u>	<u>1.6%</u>	<u>87.0%</u>
	100%	100.0%	100.0%	100.0%

Note: Based on on-site inspection of 125 projects by qualified members of the study team. Ratings are at the project level, but have been weighted by the number of units in each project.

sample appeared to our inspectors to need further major repairs to meet HQS criteria or local code requirements.

Reasons that additional repairs were still required varied across the sample, with no one reason the dominant factor. For example, two cities drew up contract specifications that were so strict in their interpretation of allowable repairs that, in the opinion of our inspector, eight of the ten properties sampled required minor additional repairs, primarily to drywall and subfloor, roofs, exterior unit surfaces, and yard areas. In two of the eight projects with major deficiencies after rehab, cities knowingly chose to renovate occupied projects even though extenuating circumstances prevented fully meeting HQS. In three projects, the contractor failed to complete the specified work in an adequate manner, and final payment should not have been made; and in the three remaining properties, the problem clearly lay with a failure to include all necessary work in the specifications.

Significantly, three of the five programs with recurring problems in project quality and completeness were among the seven highest ranked performers in our sample according to HUD's program indicators, and a fourth was in the top 12.¹ Quality problems such as these cannot be revealed without on-site inspection; nevertheless, in measuring program performance or making funding adjustments, it would be desirable if quality factors could in some way be taken into account.

1. HUD's original performance scoring system (presented in the Federal Register, December 10, 1985, 24 CFR Part 511) calls for each site to be assigned a composite score, giving equal weight to the six performance factors identified in Chapter 1 of this report.

Notably, 70 percent of the units with below average ratings on both the quality and scope of work were in localities where owners were responsible for preparing the work specifications. In contrast, owners prepared the specifications for only 37 percent of the units without major problems. In most instances, an experienced specification writer would probably have avoided the problems that arose. Although some construction problems resulted from streamlining the specification process, making the owner responsible for drawing up specifications nevertheless worked well in many other communities. Seven of the 14 sites that streamlined in this way produced uniformly sound finished units, and only one had a problem with an owner-expanded scope.

Units that were rehabilitated through RRP within a few months after they were purchased accounted for 14 percent of all projects and 18 percent of all units; yet they included one-third of the projects with major quality and completeness problems and 36 percent of units where further minor repair would have been desirable, although not necessarily economically justifiable, after rehab. Furthermore, over 62 percent of units purchased immediately prior to rehab under the RRP would have benefitted from minor or major repairs after rehab. As detailed in Chapter 5, these units were also much more frequently gut rehabs, had substantially higher rehab costs per unit, and received an average of more than twice as much public subsidy as other units. The RRP is a shallow subsidy program that was intended for use in moderate rehab. Based on the frequency of problems with projects that strayed from this intent, HUD may want to prescribe screening criteria that

localities must apply before using RRP to fund these more extensive rehab jobs.

6.3 The Composition of Rehab Costs

The average unit in the sample had rehabilitation costs of \$9,980 per unit, which was virtually the same as the average costs of all completed projects in the 34 sites (\$9,978). Forty-one percent of all units had rehab costs that were between \$2,000 and \$6,000, 23 percent had costs between \$6,001 and \$10,000, 30 percent had costs between \$10,001 and \$20,000, and 6 percent had costs in excess of \$20,000 (see Exhibit 6.4). The cost spread is partially the result of regional cost variations. When rehab costs are adjusted using the Dodge construction cost index, the mean cost per unit rises to \$10,562, but the variance in cost is reduced by one-third. Expenditures of \$6,000 to \$8,000 are notably uncommon for no apparent reason. It may be that localities either encourage doing the maximum amount of rehab that they will match or encourage very modest rehabs. Both strategies would discourage expenditures in the middle range.

Based on a review of contract documents and other information contained in project files, rehabilitation costs in the 125 sample projects were broken down into three broad categories: (1) expenditures required to meet local codes and/or Section 8 HQS; (2) expenditures required for other improvements our inspectors felt were "essential" to sound management and marketability; and (3) general property improvements (GPIs). Guidelines that were used by our rehab specialists to allocate hard-to-classify items and the items classified as other essentials or GPIs are described in Appendix C and in Section 6.3.1.

EXHIBIT 6.4

**DISTRIBUTION OF UNITS BY TOTAL REHAB COSTS, BEFORE AND
AFTER ADJUSTMENT FOR REGIONAL COST VARIATIONS**

<u>Cost Per Unit</u>	<u>Unadjusted</u>	<u>Dodge Adjusted</u>
\$2,000 or less	0.0%	2.7%
2,001 - 4,000	25.2%	13.5%
4,001 - 6,000	15.7%	17.5%
6,001 - 8,000	4.0%	5.0%
8,001 - 10,000	18.7%	10.2%
10,001 - 12,000	16.5%	16.7%
12,001 - 15,000	8.3%	14.6%
15,001 - 20,000	6.1%	11.9%
20,001 - 30,000	2.9%	6.3%
Over 30,000	<u>2.6%</u>	<u>1.6%</u>
	100.0%	100.0%

Note: Based on the 125 sample projects examined on-site, weighted with unit weights.

According to these estimates, rehabilitation costs are dominated by expenditures which were required to meet local codes and/or HQS. As shown in Exhibit 6.5, such expenditures averaged \$9,445 per unit, and account for about 95 percent of total costs. Almost 43 percent of all units incurred expenditures for other repairs essential to sound management and marketability, but these improvements accounted for only 4.7% of total cost. Similarly, about 6 percent had costs attributable to general property improvements, but such improvements accounted for only 0.7% of total costs. Overall, costs in excess of code/HQS were relatively modest, averaging about \$1,045 per unit when such costs were incurred, and only about \$465 in the sample as a whole. Less than one percent of all rehab costs were for general property improvements (GPIs) which, in the opinion of our inspectors, exceeded standards for modest housing or were not housing-related. Two of the five projects with GPIs were luxury-quality rehabilitations, two added solar hot water heaters at the locality's urging, and one provided new electrical service to a commercial area.

The low level of expenditures for repairs beyond those needed to meet code and HQS suggests that allowing localities to exercise discretion over what repairs to fund generally did not result in diversion of much funding from creation of modest housing. Typically, discretion instead allowed localities and owners to specify a few low-cost improvements that made the properties easier to manage and market. This finding should be tempered with a recognition that our inspectors assessed whether each expenditure was to repair or replace an item that failed HQS or local code requirements. Except in a very few

EXHIBIT 6.5

COST PER UNIT BY NATURE OF COST AND FREQUENCY INCURRED

<u>Cost Category</u>	<u>Average Cost Per Unit</u>	<u>Percentage of Total Costs</u>	<u>Percentage of Units</u>	<u>Average Costs for Units Incurring Expenditures</u>
Code/HQS Expenditures	\$9,445	94.6%	100.0%	\$9,445
Other Essential Repairs	465	4.7	42.7%	1,045
General Property Improvements	70	0.7	6.3%	970
Total Rehab Costs	\$9,980	100.0%	100.0%	\$9,980

Note: Based on 125 sample projects visited on-site, weighted with unit weights.

instances where the materials or methods used were too costly to be appropriate in modest-cost housing, all expenditures on those items were classified as code/HQS. In some cases, then, it is possible that an adequate remedy could have been effected a little more cheaply than the one actually carried out, for example, through repair rather than replacement. Such decisions, however, are inherent in the rehab process, and our inspections did not attempt to second guess them.

6.3.1 Costs of Other Essential Repairs and GPIs

Exhibit 6.6 shows the distribution of expenditures for other repairs essential to sound management and marketability and GPIs by the level of costs required to meet code/HQS. While expenditures over and above code/HQS were relatively common at all levels of code/HQS expenditures, their amount varied significantly. In general, the largest expenditures on other essential repairs and GPIs were found in projects with relatively low code/HQS costs. Conversely, units with relatively high costs associated with meeting code/HQS standards generally had negligible expenditures on other kinds of improvements.

Local judgment about the need for repairs to meet code/HQS often differed from the judgment of our rehab specialists.¹ Only 16 of

1. Three localities rated carpet as a general property improvement, which often prevents these expenditures from counting toward the rental rehab match, and one rated downspouts and gutters in this category. Appliances that we rated as other essential items included garbage disposals, range hoods, and laundry equipment. Unit reconfiguration not required to accommodate an existing tenant, security systems, air conditioning, and utility separation were items that we always coded as other essential repairs; but some localities instead classified as code or HQS items. Some localities judged that appliances were essential to sound management and marketability, but were not required by code or HQS in their market. Finally, we reclassified many exterior surface restorations, generally with stucco or cedar shake shingles, as of a higher quality than was required to meet code or HQS.

EXHIBIT 6.6

DISTRIBUTION OF REPAIR COSTS RELATED TO CODE OR HQS VERSUS COSTS OF OTHER ESSENTIAL REPAIRS AND GENERAL PROPERTY IMPROVEMENTS
(percentage of units rehabbed)

Code/HQS Costs (per unit)	Proportion of Units With Expenditures Beyond Code and HQS Items	Cost of Other Essential Repairs and GPIs (Per Unit)					Total
		None	\$1-\$500	\$501 to \$1,500	\$1,501 to \$3,000	Over \$3,000	
\$ 2,000 or less	0.57	2.0				2.7	4.7
\$ 2,001 - \$ 4,000	0.36	16.5	4.6	4.0	0.7		25.8
\$ 4,001 - \$ 8,000	0.63	7.2	4.5	3.9	2.3	1.6	19.5
\$ 8,001 - \$12,000	0.46	16.8	7.0	6.9	0.4		31.1
\$12,000 - \$15,000	0.47	5.5		3.6	0.4	0.9	10.4
Over \$15,000	0.47	4.5	2.7	0.4	0.9		8.5
TOTAL	0.47	52.7	18.7	18.7	4.7	5.2	100.0

Note: Based on the 125 sample projects examined on-site, weighted with unit weights.

the 52 properties that we felt had "other essential repairs" or "general property improvements" were similarly classified by local staff. Furthermore, the specific items involved differed in 13 of the 16 cases. Conversely, local records showed that other essential repairs or general improvements were made at nine properties where we felt only HQS items had been addressed. Despite these differences in the classification of specific items, the overall conclusions are much the same if one adopts the local breakdowns of rehab costs. According to these breakdowns, expenditures required to meet code or HQS averaged about \$9,582 per unit, or about 96 percent of total costs.

In addition to the expenditures reported here, 36 percent of the projects with 34 percent of the units involved owner expenditures on rehab above and beyond those required by the rental rehab program. Such expenditures averaged about \$512 in the sample as a whole, and about \$1,790 for units that incurred such costs. Some of these expenditures were required to resolve unanticipated problems with code or HQS, and one owner enhanced two projects (containing one percent of all units) with luxury items funded separately from the rental rehab work. For the most part, however, the expenditures resulted from the fact that, like our inspectors, many owners still perceived the need for some minor property improvements or repairs after the major renovation was complete.

6.3.2 Costs By System Element

Exhibit 6.7 shows the relation between the number of major systems overhauled or replaced and the rehab cost per unit. Generally, the number of major systems overhauled rises with the cost of rehab.

EXHIBIT 6.7

COST PER UNIT BY NUMBER OF MAJOR SYSTEMS OVERHAULED OR REPLACED

<u>Cost per Unit</u>	<u>Number of Major Systems Overhauled/Replaced</u>					
	<u>0</u>	<u>1</u>	<u>2</u>	<u>3-4</u>	<u>5-6</u>	<u>7-8</u>
Under \$4,001	8	10	1	1		
4,001 - 6,000	4	4	3	4	3	
6,001 - 8,000		4	2	2		
8,001 - 10,000		5	3	6	4	1
10,001 - 15,000	1	3	2	15	13	5
15,001 - 20,000			1	6	3	2
20,001 - 30,000					3	3
Over 30,000						3

Note: Based on the 125 sample projects examined on-site, weighted with unit weights.

However, a few projects repaired or replaced most major systems at a low cost per unit, and a few overhauled relatively few systems at an above average unit cost. When total rehab costs were below \$4,000 per unit, the rehab work was always relatively minimal. Conversely, when it exceeded \$20,000, the majority of systems were replaced.

Exhibit 6.8 shows the average cost per unit by type of work performed. Separate costs are provided for units where work of a particular type was done and for all units combined (i.e., regardless of whether funds were spent for that type of work). The percentage of units with expenditures in each cost category and the percentage of expenditures that funded items needed to meet code or the Section 8 Housing Quality Standards also are shown.

The largest expenditures, roughly \$2,500 per unit, were for interior unit surfaces. This was also the most common type of work, with 92 percent of all units reporting expenditures in this category. The next most important category was building exteriors, where 84 percent of the sample units spent an average of \$1,600. HVAC, plumbing and electrical repairs were also relatively important, averaging between \$600 and \$800 in the sample as a whole. At the other extreme, expenditures on relocation and on commercial space were fairly minimal, and no funds were spent adapting units for handicapped use. The only expenditures that frequently went for items that exceeded code or HQS requirements were related to security or to the repair of auxiliary structures such as garages.

EXHIBIT 6.8

COST PER UNIT BY SYSTEM REPAIRED

System	All Units		Units With Work	
	Average Cost Per Unit	Percent of Units With Work	Average Cost Per Unit	Proportion of Costs Attributable to HQS/Code
Building Exterior	\$1,347	84%	\$1,612	90%
Foundation/Structure	302	36%	848	95%
Roofs/Gutters	475	59%	803	100%
Auxiliary Structures	248	40%	622	77%
Heat/Ventilation/A.C.	699	68%	1,066	90%
Kitchen	868	83%	1,045	95%
Bath	590	77%	764	99%
Electric *	787	80%	986	99%
Plumbing *	627	69%	903	98%
Interior Common Areas	168	31%	544	93%
Interior Unit Surfaces*	2,467	92%	2,685	94%
Windows	513	75%	681	99%
Security/Safety	134	53%	251	80%
Energy Conservation	341	67%	510	100%
Extermination	57	31%	186	100%
Handicapped Adaptations	-	-	-	-
Commercial Space	11	1%	401	100%
Demolition	321	39%	826	100%
Relocation	1	1%	102	100%
TOTAL	\$9,956	100%	\$9,956	95%

Based on the 125 sample projects examined on-site, weighted with unit weights.

* Excludes expenditures on the bathroom and kitchen systems.
 Note: Overhead, profit and other soft costs have been allocated proportionally across the systems with expenditures.

6.4 Factors Influencing Rehab Cost

Several factors influenced the overall level of rehab costs. Not surprisingly, pre-rehab condition had a very large impact. As shown in Exhibit 6.9, each step down in condition equated to at least a \$5,000 increase in unit rehab costs. The high costs of uninhabitable properties, which constituted roughly 20 percent of the units completed to date, either required owners to contribute substantially more than half of the rehab amount or the community to supplement the RRP grant with other public funds. As is evident from the chart, the latter was typically the case. Rehab involving unit reconfiguration or addition also had significantly higher costs (\$15,542 per unit compared to \$8,833) and a higher concentration of supplemental public funding.

Many other factors may influence rehab costs. One group of factors relate to the property and the rehab work. Exhibit 6.9 shows that buildings in the program typically cost more to rehab if they were old, had less than 10 units, or had three or more bedrooms per unit.¹ High quality rehab costs more than the roughly equal cost for rehab of average or poor quality, which suggests that rehabbing to a high quality standard was a preplanned decision, but that poor rehab quality was more likely a result of a bad choice of contractor. Rehab costs per unit were not significantly different in neighborhoods that were improving, stable, or declining.

A second group of factors relate to rehab management and financing. To examine these factors, two variables about rehab

1. Factors are considered influences if they were statistically significant cost differences at the 95 percent confidence level or better according to t-tests.

EXHIBIT 6.9

**INFLUENCE OF REHAB CONDITION AND UNIT RECONFIGURATION
ON COSTS AND SUBSIDY LEVEL**

	<u>Average Per Unit Rehab Costs</u>	<u>Total Public Contribution Per Unit</u>	<u>Ratio of Total Public Contribution to Rehab Costs</u>
<u>Pre-Rehab Condition</u>			
In Need of Limited Repairs	5,324	2,630	.46
Dilapidated	10,618	5,678	.50
Uninhabitable	17,948	8,541	.48
<u>Unit Reconfiguration/Addition</u>			
Projects With Such Work	\$15,542	\$7,287	.50
Projects Without Such Work	8,833	4,564	.48

Note: Based on the 125 sample projects examined on-site, weighted with unit weights.

management were coded from the data collected. The first -- whether the locality was strict, intermediate, or permissive in allowing a broad range of rehab in the scope of work -- was based on whether the locality:

- o often defined items (other than unit reconfiguration) as code or HQS that we considered other essentials or general property improvements or ever included luxury items in work scopes;
- o allowed owners to draw up work scopes and these often included other essential rehab;
- o defined many things that we considered code or HQS as other essential items and did or did not allow inclusion of these items in the work scope, and
- o had a policy of allowing general property improvements in the owner's rental rehab match, as an extra expenditure beyond the match, or not at all.

The second -- whether the locality's rehab management was tight, loose, or minimal -- was based on the frequency of the following:

- o final draws being paid and contracted work never being completed;
- o properties frequently still requiring minor repair after rehab; and
- o writing or allowing owners to write specs that failed to correct/created code or HQS problems, included luxury items, or were otherwise deficient.

Exhibit 6.10 shows that experienced owners and localities were generally involved in rehabs that cost slightly more per unit. The degree of program streamlining had little effect on cost. Localities with lesser rehab competence and those that exercised little control over the breadth of work scopes, however, had much lower rehab costs per unit than other cities. These findings may suggest that complete rehab involves some items that owners, especially novices, do not consider cost-effective; competent local management is needed to assure these

EXHIBIT 6.10

BREAKDOWN OF REHAB COST PER UNIT BY SELECTED
BUILDING AND NEIGHBORHOOD CHARACTERISTICS

	<u>Cost Per Unit</u>
<u>Year Built</u>	
Pre 1940	12,159
1940-1959	9,483
Since 1960	5,193
<u>Number of Units</u>	
1 - 9	11,063
10 or more	5,629
<u>Number of Bedrooms</u>	
0 - 2	9,268
3 or more	12,437
<u>Rehab Quality</u>	
High	12,669
Average	9,264
Poor	9,777
<u>Neighborhood Trend</u>	
Improving	10,673
Stable	10,217
Declining	9,850
<u>Owner's Rehab Experience</u>	
Some	10,533
None	9,420
<u>Locality's Rehab Experience</u>	
Some	11,458
None	9,055
<u>Administrative Approach</u>	
Streamlined	10,081
Intermediate	10,666
Handholding	9,158
<u>Rehab Management</u>	
Minimal	7,458
Loose	10,312
Tight	11,437
<u>Breadth of Scope</u>	
Permissive	7,192
Intermediate	11,669
Strict	10,826
<u>Public Rehab Funds Besides RRP</u>	
Yes	14,931
No	8,463

Note: Based on a review of files related to 125 sample projects, weighted with unit weights.

improvements are undertaken. Alternatively, they may suggest that experienced owners and localities are more likely to get involved in ambitious rehab efforts and/or that localities which spend very modest amounts per unit do not find it worthwhile to exercise much control over what is done.

The influences on rehab cost are not clear cut. The cost-related property characteristics and rehab management variables relate to one another in a complex manner. To help sort out their relative influence, we ran a regression analysis on the natural logarithm of rehab cost per unit, adjusted for regional cost variations using the Dodge index. Consistent with most modeling of housing price variations, a natural log model was used to avoid the assumption that the cost variable and the explanatory variables were linearly related. Exhibit 6.11 summarizes the regression results. The model explains 66 percent of the variation in rehab cost.

One group of variables in the regression related to the rehab itself: the initial condition of the project, its age, its size, the average number of bedrooms per unit, the number of major systems overhauled, whether units were added or reconfigured, and whether the rehab work was of high quality. Five of these variables had a statistically significant impact on rehab costs. When a project was initially uninhabitable, it cost \$5,770 more per unit to rehab, while dilapidated structures cost \$4,774 more per unit. Larger projects were less costly to rehab, with the cost dropping \$222 for each unit increase in the project's size. This reduction in cost probably results from economies to scale in the rehab of common elements, roofing, and the

EXHIBIT 6.11

PROJECT, NEIGHBORHOOD, OWNER, AND PROGRAM
 FACTORS INFLUENCING COST PER UNIT REHABBED
 (ADJUSTED FOR REGIONAL COST VARIATIONS)

<u>Factor</u>	<u>Impact on Cost</u>
Pre-Rehab Condition	
Dilapidated	\$4,774***
Uninhabitable	5,770***
Number of Units	-222**
Number of Bedrooms Per Unit	1,717**
Number of Systems Overhauled	1,454***
Units Reconfigured	1,136
High Quality Rehab	528
Built Before 1940	222
Neighborhood Declining	1,541
Owner has Rehab Experience	1,794*
City has Rehab Experience	1,104
City Permissiveness (1=strict, 3=permissive)	-638
High Cost/High Vacancy Market	1,994
Low Cost/High Vacancy Market	89
High Cost/Low Vacancy Market	-1,446
Streamlined Admin Approach	-1,006
Intermediate Admin Approach	-306
Project Uses Other Public Funds	3,891***
Constant	2,204***
R ²	.66
Number of Observations	124

Key:

- *** Significant at .01
- ** Significant at .05
- * Significant at .10

building exterior. Projects where the average number of bedrooms was greater cost more to rehab, with each bedroom increasing the cost by \$1,717.

Other variables in the regression related to the local housing market, the neighborhood, and owner and program characteristics. Units where other public funds helped subsidize the rehab involved an average of \$3,891 more in rehab costs than units where RRP was the only subsidy. Owners with prior rehab experience typically spent \$1,794 more per unit on rehab. None of the remaining variables had a statistically significant impact on rehab costs.

6.5 Summary and Conclusions

The majority of RRP projects were in relatively poor condition prior to rehab. Twenty-five percent of all units were in totally vacant properties. Roughly 20 percent were rated as uninhabitable; 40 percent as dilapidated; and 40 percent as in need of limited repairs. Rehab costs and the scope of repairs were closely tied to the initial condition of the property.

After rehab, the great majority of projects provided sound, useful units for people of lower income. The quality of workmanship and materials was rated as "average" in 71 percent of the units; as "high" in 20 percent; and as "poor" in nine percent. Furthermore, about nine percent of the units appeared to need major repairs at the time of the site visit and would probably fail an HQS inspection. In all but one case, these units were the same as those which received a low rating on the quality of the work.

Allowing localities discretion in determining allowable repairs generally did not result in expenditures in excess of those required to meet local code or Section 8 HQS. Expenditures to meet HQS or code averaged \$9,445 per unit, and accounted for 94 percent of total rehab costs. Another five percent was spent on other improvements considered essential to marketability and sound management, and less than one percent went for general property improvements. In addition to the RRP expenditures reported here, 36 percent of the units involved owner expenditures on renovation work above and beyond that financed through the RRP. Factors influencing rehab costs include initial property conditions, property size, unit size, the number of systems overhauled, and the use of additional subsidy -- beyond the RRP -- to finance rehab work.

CHAPTER 7

SUMMARY AND CONCLUSIONS

This study has examined the Rental Rehab program as it was operating in mid-1986. As indicated at the outset of this report, the study was conducted at a relatively early point in the program. Although the RRP had been active for approximately two years, the program was still in its start-up phase, and numerous sites were in the process of adjusting their programs to better meet program goals. At the time of the data collection, the average site had committed 58 percent of its combined FY 1984 and FY 1985 allocations. Completions were far lower, however, with less than 10 percent of the initial allocation expended in completed projects.

While HUD has established a variety of criteria against which RRP performance can be measured,¹ the emphasis to date has been on production -- specifically dollars committed to Rental Rehab projects. This reflects both a desire on the part of the Department to ensure that RRP resources reach their intended beneficiaries as rapidly as possible, as well as a belief that localities have ample latitude to adjust their programs to local conditions and should therefore be able to achieve acceptable commitment levels.

In support of this, HUD has provided grantees with access to extensive technical assistance in various aspects of program design and

1. Six measures are defined in the Federal Register, December 10, 1985 (24 CFR Part 511), including commitment and completion rates, affordability of the units, serving large families, serving in-place tenants, minimizing public expenditures, and leveraging.

administration. The Department has also taken steps to reward sites which have achieved substantial production through the reallocation of grant funds. Within the study sample, 15 sites had their original allocations increased, while five sites had a portion of their original allocations recaptured. Fourteen sites were unaffected by the reallocation process.

Although reallocations to date have been based on commitment levels only, future reallocation decisions will be based on performance related to a number of other program objectives including the types of households served by the program, the affordability of the units produced, and the extent to which public sector costs have been minimized. As shown in Chapter 1, sites that perform poorly by one measure may perform exceptionally well by another, suggesting that there are many tradeoffs involved in the implementation of local programs. As a result, future reallocation decisions may have quite different outcomes than those that have been made to date.

This chapter reviews key findings of the study, beginning with the program design choices and operational arrangements adopted by the 34 sites. Subsequent sections summarize findings related to the tenants served, the affordability of the units, the types of owners participating in the program, and the types of rehabilitation work funded by the RRP.

7.1 Administering Agencies and Program Design

The communities selected for this evaluation include 28 cities and 6 urban counties, ranging in size from about 50,000 to over 2 million population. Typically, the program was designed and operated by

a city or county housing rehab agency, working in conjunction with an independent PHA. Other organizational arrangements included six sites where the rehab entity and the PHA were both departments of a single city or county agency, and three sites where a PHA was responsible for both the rehab and tenant assistance components of the program.

Lead agencies in the 34 sites were primarily city or county community development departments, but included a few non-CD agencies and non-profit organizations, as well as the three PHAs. Not surprisingly, there was substantial variation in their prior experience in housing rehab. However, the relationship between experience and RRP performance is not particularly strong. Focusing on two key measures of performance -- production and leveraging -- we found that sites with substantial output under prior CD programs achieve about the same level of commitments as less experienced sites, but show less success in leveraging private funds than sites with either low or moderate experience in housing rehab. By contrast, the sites with the least amount of experience tend to be concentrated in the highest performance category as measured by both production and leveraging.

Similarly, participation in the RRP demonstration does not appear to be associated with stronger performance under the program itself. Indeed, sites with Demonstration experience were underrepresented in the highest performance group, while non-participants tended to be concentrated in this category. While difficult to explain, this pattern may in part reflect the greater use of repayable subsidies among Demonstration participants. Sites that were new to the RRP concept were more likely to adopt the model promoted

by HUD, and offer subsidies in a forgivable form. As described below, the use of forgivable subsidies typically led to higher commitment rates.

Indeed, the mechanism by which the RRP subsidy is delivered proved to be one of the most important choices open to RRP grantees. Flexibility in subsidy selection presumably allows sites to gear the program to local market conditions by making the subsidy attractive enough to generate demand for the program while also holding public contributions to the minimum necessary to support needed repairs. However, program administrators may not always assess market conditions correctly. Furthermore, local politics appear to have acted as a constraint in subsidy selection in a substantial number of sites.

The types of subsidies offered by the sites included grants and forgivable loans, direct loans, deferred payment loans, and interest subsidies. Taken together, grants and forgivable loans were the most popular approach to subsidy provision, with 17 sites choosing one or the other of these non-repayable forms. Fourteen sites delivered the subsidy as a repayable loan, and three sites offered both forgivable and repayable forms. Other funds (typically CDBG) were frequently used to supplement Rental Rehab subsidies, particularly in sites that offered the basic subsidy as a loan. Altogether, 21 of the 34 sites offered additional public funding to at least some of their Rental Rehab projects. At the same time, very few sites attempted to minimize subsidies through the use of gap financing techniques, variable loan terms, or the imposition of a subsidy maximum lower than the 50% of cost or \$5,000 per unit cap established by the program. The sites'

reluctance to use gap financing approaches appears to reflect an important trade-off between the goal of minimizing subsidy amounts and the desire to make the program attractive to potential participants.

As noted above, the type of subsidy offered by the sites appears to have a substantial impact on program performance. Sites offering a non-repayable subsidy show higher commitment rates overall, regardless of the markets in which they are operating. However, market factors also appear to play a role, with sites operating in tight markets showing generally higher commitment rates than those operating in loose markets. Tight markets, however, are associated with the lowest overall leveraging ratios, suggesting that programs in these areas have purchased at least some of their production through the use of other funds to supplement Rental Rehab dollars.

It is also important to note that, over the two-year period covered by the study, nine of the 34 sites made adjustments to their original subsidy approach in order to increase its attractiveness to property owners and maintain an adequate flow of applications. Adjustments included switching from a repayable subsidy to a grant or forgiven DPL, reducing interest rates and/or deferring payments on direct loans, and providing additional funding from CDBG allocations. These changes most clearly reflect the tradeoffs between production and other objectives, such as leveraging or obtaining a payback from RRP monies invested. They also demonstrate the flexibility inherent in the program, which allows sites to adapt their subsidies to changing market conditions or to redesign their programs if necessary to achieve the desired results in a given market.

Another important aspect of program design is the selection of target neighborhoods. Despite the emphasis within the program on careful neighborhood selection, most programs opted to define as broad a target area as possible. The majority of the sites designated eligible areas on the basis of HUD regulations without further attempts to focus the program. Five did not designate eligible areas at all, but instead, qualified projects as applications were received based on project- or block-level data. By contrast, 13 sites selected some subset of the otherwise eligible areas in their jurisdictions, with about half of these selecting pre-designated CD neighborhoods.

The principal rationale for less restrictive targeting was a desire to cast a wide net in recruiting project owners. As with subsidy mechanisms, changes in target area designation were not uncommon. Over the 2-year period, eight sites acted to expand or abandon originally designated target areas in an attempt to broaden the base from which owners could be recruited. Nevertheless, based on data for the areas in which RRP projects are actually located, it appears that the program is generally operating in the appropriate kinds of neighborhoods. While program outcomes vary with the characteristics of RRP neighborhoods, the impact appears to be mixed, with no one neighborhood type associated with higher or lower overall performance.

Site approaches towards project selection also reflected the need to achieve or maintain an adequate flow of commitments. Program descriptions and other early documentation typically contained explicit preferences for the types of owners/projects sought, and occasionally contained rather complex scoring systems for use in project selection.

In practice, however, projects were approved on a first-come, first-served basis, and, in many cases, stated preferences could not be implemented. The only factors that appeared to play a major role in project selection were the need to avoid displacement and the size of the units proposed. Given program standards for the proportions of two and three bedroom units to be produced, projects containing larger units generally received priority.

While in concept, both neighborhood and project selection criteria are important features of program design and key elements of local discretion, in practice, the sample sites were unable to exercise much selectivity in this regard. The vast majority of the sites indicated that pressures to achieve target commitment rates, combined in many sites with a dearth of applications, resulted in the selection of virtually all projects that met basic eligibility criteria. Although most sites employed a variety of approaches to advertise the program and recruit owners, about a third described the level of applications as inadequate. While some of these sites intended to intensify their marketing efforts in order to remedy this problem, at least some were considering a redesign of the subsidy approach in order to increase its attractiveness to potential participants.

The study also examined the ways in which various roles and responsibilities have been allocated under the program, and the extent to which a "streamlined" versus a "handholding" approach has been employed in the different sites. In general, we found that RRP staffs were small, with less than 3 full-time equivalents in about two-thirds of the sample sites. Except in the larger programs, RRP staff tended to

be assigned only part time to the RRP, with other programs consuming a good proportion of the Director's time. Responsibilities for various program activities tended to be centralized in these staffs, with one or two rehabilitation specialists performing all necessary functions, occasionally obtaining specialized help from other city departments. Administrative costs were typically an indistinguishable part of CDBG administration, with no separate budget established for the RRP.

The RRP did exhibit an overall tendency towards streamlining, particularly with respect to owner responsibility for obtaining secondary financing. In the majority of sites, this was viewed as the sole responsibility of the owner, and correspondingly, few sites made any attempt to officially involve private lenders in the program. In 14 of the sites, owners were also responsible for preparing the detailed specifications of the work to be accomplished. Although the specification writing function was retained by program staff in the remaining areas, arguments for doing so were based on efficiency and speed of processing.

Based on the allocation of functions and other aspects of program processing, sites were classified along a handholding/streamlining continuum. We found that both "handholding" and "streamlined" sites had higher production and completion rates than those in the intermediate group. Nevertheless, streamliners achieved slightly better results in both regards at a substantially lower cost. Based on some rough calculations, we estimate that the average cost of administration ranged from about 2 percent of the average per unit

subsidy amount in streamlined sites to about 9 percent in sites that adopted a more "handholding" approach.

Finally, the study provides some insights into HUD's Cash and Management Information System C/MI which is used both to control disbursements to committed projects and to collect data on the progress and outcomes of the program. While the study did not explicitly focus on the funds management aspect of the system, it appeared to work well in most sites. As a data collection/program monitoring tool the C/MI also appears to provide a reasonably accurate picture of program performance. Although we detected a sizable number of errors in the reported data, the overall impact was small. Problems in C/MI reporting are already being addressed by the Department and should result in an improved data base for future program decision-making.

7.2 Role of the PHA

Because the Rental Rehab program uses two types of subsidies -- rehabilitation subsidies to property owners and rental subsidies to tenants -- the program typically requires two separate entities to cooperate in the implementation of the program. Normally responsibility for rehab functions (including program design, property selection, specification of needed repairs, and project processing) is assigned to a city/county rehab office. Responsibility for issuing certificates and vouchers to eligible tenants belongs to the PHA, typically an independent local agency. In only three of the sample sites was the entire program PHA administered.

Overall, it appears that PHAs have played a fairly modest role in the Rental Rehab program. City/county agencies generally took the

lead in program design, with only 6 of the sample PHAs indicating that they had played an "active" role. Similarly, only five of the PHAs indicated an ongoing involvement at a policy level, and only a few participated in the selection of properties or decisions regarding property repairs. Although the majority conducted a final HQS inspection, PHAs rarely took the lead. Instead, their dominant role was typically limited to matters directly related to the provision of tenant assistance.

Even within this category of activities, however, PHA functions were often fairly narrow. Specifically, in only a minority of the sites did PHAs appear to take a "managing" role with respect to overall tenant issues. PHAs were typically not involved in such activities as collecting data on initial tenants, monitoring turnover in the projects, or reporting, other than maintaining records on assisted households. Rather, reporting and monitoring functions -- to the extent these were performed -- were retained by the grantees. Although in a large number of sites the interaction between grantee and PHA staff was frequent and of a collaborative nature, in a sizeable number of sites, city staff took the lead in all aspects of tenant assistance -- including initial screening -- calling on the PHA only when specific households were ready for formal certification and the issuance of a voucher or certificate.

Overall, both city and PHA actors appeared to be satisfied with the allocation of functions between them and had developed good working relationships in carrying out their respective responsibilities. Nevertheless, some areas of tension did arise. With respect to design of the program, the most common problem was the quality of the

neighborhoods in which RRP projects were located. About twenty-three percent of the PHAs expressed concern that the neighborhoods were too deteriorated or unattractive to certificate holders. Roughly equal proportions mentioned administrative problems related to units that failed initial HQS inspections or coordination problems relating to the timing of project completion.

Despite general satisfaction with program roles -- on the part of both grantee and PHA actors -- it appears that the interaction of two different actors can work to the detriment of the program if responsibilities are not adequately specified and understood by both parties. Specifically, in one of the sample sites, we found that a misunderstanding about which actor was responsible for overall tenant issues -- including the identification of potential displacees and monitoring of tenant turnover -- had resulted in a failure to perform these functions. In general, regardless of the diligence with which grantees or PHAs appeared to perform these activities, lack of record keeping on this matter made it virtually impossible to determine the extent of displacement that had occurred under the program or to collect data on households that had moved from Rental Rehab projects. This suggests a need within the program as a whole to clarify responsibilities with regard to tenant management -- including such record keeping requirements that HUD deems appropriate -- and to ensure that these functions are clearly assigned to one of the participating actors. Again, HUD is currently in the process of addressing this issue through instructions to grantees and HUD field offices.

7.3 Program Impact on Tenants

The Rental Rehab Program is clearly serving the population of households it was intended to serve -- seventy-nine percent of all post-rehab tenants were very low income households, and another 14 percent had incomes between 50 and 80 percent of the area median. Sixty-nine percent were minorities and about half were female-headed families with children. Thus, households with the greatest overall incidence of housing needs appear to have been the primary recipients of program benefits.

The great majority of RRP units also meet the affordability standard adopted by HUD. While the average unit experienced a rent increase as a result of its renovation, particularly in buildings where rehab costs were high, the overwhelming majority of RRP units had post-rehab rents that were at or below the applicable FMR. The average unit in the sample rented for about 87 percent of the FMR, and only about 10 percent of all units had rents that were above the FMR. Thus, most units developed to date were affordable to low-income households (i.e., with incomes between 50 and 80 percent of the local median) even in the absence of assistance.

While post-rehab rents were modest, very low income households generally did require Section 8 certificates or housing vouchers to live in RRP units. Two-thirds of all post-rehab tenants received some form of rental assistance. About 82 percent of all very low income households were assisted, compared to only about 32 percent of all households with incomes between 50 and 80 percent of the local median. Forty-five percent of all rental assistance associated with the program

went to initial occupants who remained in RRP projects, 52 percent went to residents who were new, and 3 percent went to previous residents who used their certificates or vouchers to move.

In general, the overall pattern of post-rehab rents was consistent with the market orientation of the Rental Rehab program. While the ratio of rents-to-the-FMR varied with market conditions, it did not depend on the level of rehab costs, the size of the rent increase, or the amount of public subsidy. Such outcomes reflect the basic philosophy of the RRP program, which lets the market -- and not the local administrative agency -- determine project rents.

The program has been less successful, however, in meeting HUD's objective of serving low income households in place. Only about half of all post-rehab tenants had lived in the project prior to rehab. In part, this reflects the development of vacant properties. About 25 percent of all units were in buildings that were unoccupied at the time of rehab. However, it also reflects a relatively high rate of tenant turnover during renovation. Twenty-eight percent of all pre-rehab tenants moved out of their dwelling units before the renovation was complete.

The quality of the data do not enable us to assess the extent of displacement that has occurred to date. In general, households who moved out of RRP projects tended to have higher incomes than those who stayed or than those who took their places. While mobility rates were higher in projects with above-average rent increases, the fact that movers were replaced with lower income households tends to temper a

displacement argument. Information on reasons for moves, while incomplete, also does not suggest displacement.

Nevertheless, the potential for displacement certainly exists. About 15 percent of all very low income households initially living in RRP projects moved and were apparently not offered assistance. This figure could understate the level of mobility that actually occurred if moves were made before the project was formally accepted into the program.¹ Furthermore, many sites made little, if any, effort to contact tenants during the initial stages of renovation or to monitor household turnover. Such monitoring needs to be strengthened in order to ensure that tenants are aware of their options under the program.

7.4 Private Sector Response

The Rental Rehab Program has primarily attracted individual owners of smaller properties with relatively modest renovation needs. The average unit was in a building with four or five apartments and cost about \$10,000 to rehabilitate. Sixty percent of all units were owned by individuals, with partnership and trusts the next most common ownership forms (accounting for 17 and 13 percent of the sample, respectively).

While about 17 percent of all units were acquired specifically for the program, the typical investor used the RRP for the renovation of a previously held property. Fifty-eight percent of project owners indicated that the RRP grant or loan was the primary reason for their

1. By its nature, pre-rehab mobility would be extremely difficult to document; therefore, such data collection was not attempted as a part of this study.

participation. However, the remaining 42 percent viewed the Section 8 subsidy as at least as important as the rehab subsidy.

Forty-three percent of the cost of the average unit was supported by the RRP grant or loan; another 9 percent was funded by other public programs; and the remaining 48 percent was covered by private funds. While only 25 percent of all units received public funding in addition to the RRP contribution, such units had substantially higher rehab costs (over \$14,000 per unit) and substantially lower leveraging ratios (each dollar of public funds was matched by less than \$0.40 in private contributions). Private contributions were more or less evenly divided between private loans and owner's equity. When private loans were used, they were generally associated with higher rehab costs.

Since conventional leveraging ratios do not reflect the underlying value of the different subsidy types to project owners, we also calculated the net present value of the public subsidies provided by the programs. These averaged \$3,662 per unit for RRP grants and loans, and \$4,618 per unit for all public funds combined. These represent 40 and 46 percent, respectively, of the average project's rehab cost, and exhibit far less variation than conventional leveraging ratios. The net present value of forgivable DPLs (\$5,506 per unit) was about 45 percent higher than the value of repayable loans (\$3,804 per unit).

Based on survey responses of owners, three-fourths of the units would have undergone some or all of the rehab work performed under the RRP even in the absence of assistance. However, in only one-fourth of

all units would the owner have completed all of the work, and in most cases, renovations on these units would have been completed incrementally rather than all at once if RRP assistance had not been provided.

Analysis of project financial conditions confirmed that complete renovations would not have been financially feasible for most units in the absence of RRP assistance. Almost half of all units would have generated negative cash flows if the total rehab effort had been supported with private financing, and two-thirds would have had cash flow to revenue ratios under 10 percent. Nevertheless, subsidy levels were not effectively tailored to project financial conditions, and in many cases, cities provided larger subsidies than the minimum required to make rehab financially feasible. While greater use of gap financing techniques could have helped to minimize subsidies, sites evidently viewed this as a trade-off, preferring a straight 50 percent-of-cost approach that was both attractive to potential participants and easy to administer.

7.5 Nature and Cost of Repairs

Roughly 20 percent of the units renovated under the program were uninhabitable prior to rehab, 40 percent were dilapidated, and 40 percent were in need of limited repairs. The average unit had major work performed on 3.4 systems, with 5 or 6 systems typically overhauled or replaced in dilapidated and uninhabitable projects. The electrical, bathroom and HVAC systems were most frequently overhauled. In about 17 percent of the projects, units were added or enlarged, apparently in response to the program's emphasis on large units.

After rehab, the great majority of projects provided sound, useful units for people of modest income. Our rehab specialists rated the quality of workmanship and materials as "average" in 71 percent of the units and "high" in 20 percent. Only about 9 percent had "poor" quality ratings. In this respect, the RRP clearly has succeeded in producing quality work. In about 25% of the units, while code and HQS requirements were met, our inspectors felt that additional minor repairs would have improved the marketability or operating efficiency in the units. However, about 9 percent of the units still needed major repairs at the time of the site visit and would probably not meet HQS. In all but one case, these units were the same as those which received a poor quality rating on the work that was done.

Significantly, 70 percent of the projects where both the quality and scope of work were poor were in localities where owners were responsible for preparing the work specification. However, making the owner responsible for drawing up the specifications apparently worked quite well in other communities. Seven of the 14 sites that streamlined in this way produced uniformly sound finished units, and only one had a problem with an owner-expanded scope.

Allowing local flexibility in determining eligible repairs generally did not result in the use of funds for work other than that necessary to create sound housing for lower-income households. Expenditures to meet HQS and code requirements averaged \$9,445 per unit, and accounted for 94 percent of total rehab costs (\$9,980). Another five percent was spent on other improvements considered essential to marketability and sound management, and less than one percent went for

general property improvements. Costs in excess of code or HQS were incurred in about half of all units but were relatively modest.

In addition to the RRP expenditures reported here, 36 percent of the units involved owner expenditures on renovation work above and beyond that required by the RRP. Such expenditures averaged about \$500 in the sample as a whole and about \$1,800 for units which incurred such costs. Some of these expenditures were required to resolve unanticipated problems with HQS, and one owner enhanced two projects (containing one percent of program units) with improvements inconsistent with moderate income occupancy. For the most part, however, the expenditures resulted from the fact that many owners still perceived the need for some finishing touches after the RRP work was completed.

Rehab cost per unit was largely determined by the rehab work required. Significant explanators were project size, average unit size, pre-rehab condition, and the number of major systems overhauled. Rehab costs were higher in projects where the owner had some prior rehab experience. They also were higher in projects where localities supplemented RRP funds with other public monies, either because localities offered extra subsidies to more costly projects or because availability of deeper subsidies encouraged owners to pursue more extensive rehab jobs.

7.6 Overall Program Performance

As noted throughout, specific program outcomes in a given community are closely related to the type of subsidy provided, the level of rehab funded, the characteristics of neighborhoods in which projects are located, and the strength of the local housing market. However, no

one approach or market type is clearly superior to all the rest if one considers the range of program objectives established by HUD. While relatively few sites have been highly successful in all performance categories, most have done well on at least a subset of the RRP's major goals. This observed variation in outcomes is neither surprising nor inappropriate, given the diversity of local conditions, priorities, and needs.

Thus, overall, the Rental Rehab program appears to be working well. While initial production has been relatively low, it has accelerated in recent months, and many sites have made adjustments to their programs which should improve performance in this regard. As noted above, tenant monitoring should be strengthened. Nevertheless, the types of households being served, the initial affordability of the rehabilitated units, and the completion of appropriate repairs all conform to established national objectives.

The overall performance of the program will ultimately be judged on the extent to which it continues to provide quality housing at an affordable price for low income households in the years to come. While the timing of the evaluation necessarily limits our ability to assess the long-term affordability of RRP units, our findings do provide some indirect evidence on this issue.

The majority of RRP projects developed thus far have been in neighborhoods where incomes and rents were relatively low. For example, average family income in the median RRP neighborhood was only about 66 percent of the local median in 1980. Furthermore, roughly half of all RRP units developed had rents that were less than 90 percent of the

applicable FMR, and another 10 percent had rents between 90 and 95 percent of the FMR. Given a relatively low rate of inflation, such units are likely to remain within an affordable range over the next few years.

More problematic are the units with rents which are currently close to or above the FMR. As these units turn over, very low income households could well be replaced by somewhat higher income tenants unless PHAs make a concerted effort to direct certificate and voucher holders to these projects. Nevertheless, given the nature of RRP neighborhoods, as well as the modest quality of the units developed thus far, even these projects would seem likely to retain their low income character in the next few years.

APPENDIX A

SAMPLE DESIGN AND DATA WEIGHTING

Sampling for this study was conducted in two stages. In the first stage, 35 Rental Rehabilitation Program grantees were selected for site visits. In the second stage, 125 properties (i.e., projects) at the sample sites were selected for detailed analysis. This Appendix first describes the procedures used to select the sample and the tests used to assure the sample's representativeness. The weights to be used with the data collected then are presented and their use is explained.

A.1 Grantee Sample

Among the 404 cities and urban counties that received grants, budget considerations require restricting the study sample to 35 grantees. Prior to designing the sample, a decision was made to include New York City, which received by far the largest amount of grant dollars and used them in a unique manner. New York City was documented in a case study, rather than as part of the main data collection and analysis effort. Since a principle objective of the study was to examine program outcomes, we also decided not to sample sites that had not yet completed a project (C/MI status 4 or 9) at the time that the sample was generated (March 31, 1986). This restriction eliminated 109 out of the 403 communities initially participating in the program (excluding New York City), or about 27 percent of all recipients. Exhibit A.1 shows the distribution of grantees with and without completions by grant size.

The project was going to focus its outcome discussion at the grant dollar rather than the grantee level, which suggested sampling

EXHIBIT A.1
NUMBER AND PERCENTAGE OF GRANTEES WITHOUT COMPLETED PROJECTS
AS OF MARCH 31, 1986, BY SIZE OF GRANT

<u>Grant Size</u>	<u>Total Grantees*</u>	<u>Grantees Without Completions</u>	<u>Percentage Without Completions</u>
Under \$400,000	309	82	27%
\$400,000 - \$1,000,000	67	19	28%
Over \$1,000,000	<u>33</u>	<u>8</u>	<u>24%</u>
TOTAL	403*	109	27%

*Excludes New York City

grantees with probabilities proportional to the size of their grants (PPS). This sampling strategy increases the representation of grant dollars in the sample over their expected representation in a simple random sample where small grantees would dominate and few large grantees would be included. Although one could achieve a similar effect by using a random sample stratified by grant size, the PPS sample provides greater precision for the outcome estimates.

A.1.1 The Sampling Procedure

Site visits were to be conducted at 34 localities. In order to allow for possible non-response, 35 localities were sampled. The analysis, locality weights, and number of properties selected from each were based on the 34 localities actually visited.

The 294 entitlement localities with completed projects received a total of \$141,150,474 in Rental Rehab grants in 1984 and 1985. This figure divided by 35 (the number of localities to be sampled) yielded a sample interval of \$4,032,871. Three of the 294 localities had grants that exceeded this interval: Chicago (\$10,679,900), Los Angeles (\$9,112,800), and Philadelphia (\$4,706,600). Because their grants exceeded the sample interval, these cities were included in the 35 city sample "with certainty."

The grants to Chicago, Los Angeles, and Philadelphia were summed (24,499,300) and subtracted from \$141,150,474, the total grant to all 294 cities with completed projects. The difference of \$116,651,174 was divided by 32 (the number of communities still to be added to the sample), yielding an interval of \$3,645,349. Detroit's grant of \$3,669,400 slightly exceeded this interval, and Detroit was added to the

other three cities included with certainty. Subtracting Detroit's grant from \$116,651,174 yielded a difference of \$112,981,774, which, divided by 31, produced a final sample interval of \$3,644,573.

The remaining 290 communities then were sorted according to four criteria: grant size category, grantee type (city or county), HUD region, and then randomly. Three grant size categories were used, including grants of more than \$1,000,000, grants of between \$400,000 and \$1,000,000, and grants of less than \$400,000. Thus, the listing from which the sample was drawn started with cities in the Boston region receiving grants of more than \$1,000,000 and ended with counties in the Seattle region receiving grants of less than \$400,000. Communities of the same type (city or county) in the same grant stratum and region were sorted randomly, using the fourth digit from the right in the grant amount.

The additional 31 cities were chosen from this sorted list of 290 communities by starting with a random number between 1 and 290. Starting, for example, with the 156th city on the list, the program went through the list of cities adding up grant amounts. When the sum of the grant amounts equalled or exceeded \$3,644,573 (the sample interval), the community with the grant that put the total over the interval was included in the sample. The sample interval then was subtracted from the running total of grant amounts after the sampled city was added, and the program continued adding grant amounts until the interval again was reached and another community was added to the list. This proceeded until the entire list of 290 cities was gone through and 31 cities were added to the four included with certainty.

We drew three samples and ran marginals that compared them with all rental rehab communities to find the most representative sample. Exhibit 1.1 lists the 34 study participants from the most representative sample and indicates their grant amounts. The 35th site selected, Concord, CA with a grant amount of \$108,800, was dropping out of the program and declined to participate in the evaluation. Excluding New York City, the 34 localities visited were initially allocated 34.3 percent of all RRP grant funds in fiscal years 1984 and 1985.

A.1.2 Tests of Sample Representativeness

The sample was compared with the universe and was found to be representative. Tests that were performed included comparison of the sample with both the universe of all cities and counties that are entitlement recipients of Rental Rehab grants and the universe of all jurisdictions with completed projects on locality type (city or county), on region of the country, on percentage of funds so far committed to projects, and on experience in the Rental Rehab Demonstration. An additional test compared the sample with the universe of all entitlement localities on a factor tied to the program allocation formula (percentage of rental housing with lower income head of household that was built before 1940).¹ On each of these criteria, the sample was found not to be significantly different from the universe described.

1. Comparisons were not made between the sample and the rest of communities with completions on allocation factors because of lack of compatibility between data sets. Program factor data, while automated, do not have the same locality identifiers as the C/MI system. Thus, identifying the 294 communities with completions would have been a laborious manual process.

The sample is weighted on grant amount, and larger grantees intentionally are over-represented. For this reason, tests of representativeness related to population, grant amount, or other factors expected to vary with locality size are inappropriate in appraising this sample. Exhibits A.2 through A.9 document the comparisons that were performed. Additional tests that compared average number of units in started projects between the sample and all Rental Rehab entitlement communities with completions and with starts are discussed below.

Exhibit A.2

Sample Compared with Entitlement Universe on Community Type

<u>Community Type</u>	Community is:				<u>Totals</u>	
	<u>In Sample</u>		<u>Not in Sample</u>		<u>Number</u>	<u>Percent</u>
	<u>Number</u>	<u>Percent</u>	<u>Number</u>	<u>Percent</u>		
City	29	83%	279	76%	308	76%
County	6	17	89	24	95	24
Totals	35	100%	368	100%	403	100%

$$x^2 = .870$$

$$\text{significance} = .652$$

Exhibit A.3
Sample Compared with Universe of Entitlements
with Completions on Community Type

Region	Community is:				Totals	
	In Sample		Not in Sample		Number	Percent
	Number	Percent	Number	Percent		
Northeast	7	20%	94	25%	101	25%
South	9	26	106	29	115	29
Midwest	10	28	76	21	86	21
West	9	26	92	25	101	25
Totals	35	100%	368	100%	403	100%

$$x^2 = 1.44$$

significance = .305

Exhibit A.4
Sample Compared with Universe of Entitlements
with Completions on Region

Region	Community is:				Totals	
	In Sample		Not in Sample		Number	Percent
	Number	Percent	Number	Percent		
Northeast	7	20%	58	22%	65	22%
South	9	26	79	31	88	30
Midwest	10	28	62	24	72	25
West	9	26	60	23	69	23
Totals	35	100%	259	100%	294	100%

$$x^2 = .671$$

significance = .120

Exhibit A.5
Sample Compared with Entitlement Universe
on Experience in the Demonstration

Demo Experience?	Community is:				Totals	
	In Sample		Not in Sample		Number	Percent
	Number	Percent	Number	Percent		
Yes	16	46%	168	46%	184	46%
No	19	54	200	54	219	54
Totals	35	100%	368	100%	403	100%

$$x^2 = .000$$

significance = .000

Exhibit A.6
Sample Compared with Universe of Entitlements
with Completions on
Experience in the Demonstration

<u>Demo Experience?</u>	Community is:				<u>Totals</u>	
	<u>In Sample</u>		<u>Not in Sample</u>		<u>Number</u>	<u>Percent</u>
	<u>Number</u>	<u>Percent</u>	<u>Number</u>	<u>Percent</u>		
Yes	16	46%	75	33%	91	35%
No	19	45	149	67	168	65
Totals	35	100%	224	100%	259	100%

$\chi^2 = 2.00$ significance = .850

Exhibit A.7
Sample Compared with Entitlement Universe
on Percent of Program Funds Committed

<u>Group</u>	<u>Number</u>	<u>Mean Value</u>
In Sample	35	51%
Not in Sample	368	50%

T Value = .24 significance = .19

Exhibit A.8
Sample Compared with Universe of Entitlements
with Completions on
Percent of Program Funds Committed

<u>Group</u>	<u>Number</u>	<u>Mean Value</u>
In Sample	35	51%
Not in Sample	368	50%

T Value = .24 significance = .19

Exhibit A.9
Sample Compared with Entitlement Universe
on Percent of Rental Units with Lower Income
Head of Household Built before 1940

<u>Group</u>	<u>Number</u>	<u>Mean Value</u>
In Sample	35	30%
Not in Sample	368	27%

T Value = .82 significance = .59

A.2 The Property Sample

Property-level data were to be collected only at localities in the sample. Although 125 properties would be examined, the group of properties from each grantee would have to be treated as a single data element for analysis because they were a second stage sample.

A.2.1 Sampling Procedure

The implications of this approach to selecting properties were: (1) the overall sample size would benefit from a heavy property sampling for the grantees that were selected with certainty, but this increase had to be balanced against the reduced accuracy of the estimates for the sample grantees, and (2) the precision of the estimates would be maximized if the information about each grantee's properties was estimated with roughly equal precision, since each grantee's properties would be treated as a single sample observation. Thus, if there were large numbers of properties per grantee, the best sampling strategy would be to select three projects randomly from each grantee and a fourth from the grantees with the largest number of projects. (This result holds because the precision of the estimate is

much more sensitive to the absolute sample size than the proportion of the population sampled when the sample size is so small.)

In the 35 city sample, a total of 243 properties had been completed as of March 31, 1986. This total comprised 180 properties for which the final project report had been received by HUD and 63 properties for which the final draw had been made, but for which the final report still was pending. Because grantees had 90 days from the final draw until the final report was due to HUD, we assumed that by the time the property sample was selected, complete data would be available for all 243 properties.

Exhibit A.10 shows the distribution of completed properties within the 35 city sample. The maximum number of completions at a sample site was 26.

Exhibit A.10
Number of Localities by Number of Completions

<u>Number of Completions</u>	<u>Number of Localities</u>	<u>Percent</u>
1	5	14%
2	4	11
3	4	11
4	2	6
5	2	6
<u>6 or more</u>	<u>18</u>	<u>52</u>
<u>Total</u>	<u>35</u>	<u>100%</u>

Given the distribution of completed properties across grantees in the sample, the best sampling strategy was to select as many properties as were available up to four from each grantee, and to supplement those by randomly sampling five from grantees with more than six completions. Since smaller properties were disproportionately completed first, at sites where properties were sampled, we stratified

the property sample by the size distribution of properties with rental rehab funding commitments. This procedure slightly reduced the small property bias. The next section describes the residual bias.

A.2.2 Tests of Representativeness

We examined some of the characteristics of the completed properties in the 35 cities to ensure that they generally were representative of Rental Rehab properties. In no test was the sample significantly different from its comparison group, although the data did indicate that projects completed on average contained fewer units than projects not yet completed. Smaller properties probably were completed first because (1) they are easier for the locality to handle and may receive priority, and (2) they take less time to complete.

In the 35 city sample, there were 8.2 units per project started, and 4.5 units per project completed. In comparing the sample with other communities that had started projects by March 1986 (371 properties outside of the sample localities), we found that the other communities have started somewhat smaller projects at 6.6 units per property. Communities with completed projects, but not in the 35 city sample, had an average of 4.1 units per completed project. Thus, the projects started and completed are somewhat smaller in other cities than in the sample cities, although t-tests showed the differences were not significant at the 90 percent confidence level. Furthermore, some of the larger units reporting the CMI as complete actually were not, so the average number of units per project visited only was 3.9. The small property difference is the gap between 3.9 units per project and 6.6.

A.3 Weighting

Various types of weights were used in generating statistics from the rental rehab evaluation's data bases. The proper weights depended on (1) the type of information we were trying to convey and (2) the unit of analysis (e.g., the city/county, all projects, sampled projects/owners, all units/tenants, sampled units/tenants, etc.).

A.3.1 Project Versus Unit Averages

When analyzing project-specific data, we distinguished between "project" and "unit" averages. For example, rehab costs per unit could be described in two different ways. We could describe the unit costs of the average project or the cost of the average unit. The first statistic would be derived by taking a simple (i.e., unweighted) average of the unit costs of every project; the latter statistic would be a weighted average of these unit costs, where the weights reflect the number of units in each project. While both concepts have their applications, most of the descriptive "project" analysis was based on unit averages.

A.3.2 Site Weights

In addition to the unit versus project distinction, our sampling plan required weighting the data in order to combine the information collected at different sites. In generating our sample, we tried to make each site represent the same approximate amount of grant dollars. If this were possible, when we found that about 10 percent of the sample sites used gap financing, we could conclude that about 10 percent of all Rental Rehab Program funds were spent this way. Because

Chicago, Los Angeles, and Philadelphia had such large grants, however, each received more funds than the uniform amount that each of the other 31 sites represented. Consequently, the data from all sites except these three were self-weighting, but these three received larger weights. Note that these larger weights do not create a large city bias in the data. They are included because these cities each received several times the amount of funding received by the groups of localities represented by the sites that did not enter with certainty. To accurately explain what was done with all grant dollars, we have to count all the funds received by the three large cities. They have most of the tenants and their tenants are counted proportionately to their presence in the overall tenant population. The tenants from small localities in the sample are weighted up to accurately represent the number of tenants in small localities in the overall program.

A.3.3 Weighting to Describe Current Accomplishments or the Eventual Use of the Average Grant Dollar

One problem facing the evaluation was that the Rental Rehab Program still was in its infancy. Our sampling was based on how the grant dollars were allocated. Implicitly, our weighting of the data assumed that the dollars spent at the time of our site visits were spent in the same way that subsequent dollars would be spent.

For administrative issues, this assumption was reasonably valid, and we collected data about those rare cases where it was not. (Recall the data about recent and planned changes in the local programs.) For analyses of funding commitments, this assumption also was credible. For analyses involving completed projects and their

occupancy, however, this assumption was unavoidably flawed. The program was still so young that the projects completed were disproportionately the small ones. When sites had a large number of completions, we compensated for this problem by sampling projects that were representative of the commitments. However, we were forced to select all completed projects at the majority of sites. In several cases, all the completions were one to four unit projects, but the bulk of the locality's funds were committed to larger projects.

We could have dealt with rehab/post-rehab data on projects/units/tenants in two ways. One approach was to present a profile of completions at the time of our sites visits. We rejected this approach because the estimates would have an extremely high standard error, with data from some projects being weighted as much as 80 times data from others. The sample was not designed to reliably support this approach.

The second approach, which we adopted, was to weight the data in the way we intended when we drew the sample, but warn the reader of the small property bias in our estimates. This approach yielded the estimates with the smallest standard error. In effect, it described the probable characteristics of the average project/unit/tenant once all grantees have spent the funds that were allocated at the time of our site visits. It relied on the assumption that completions and commitments at that time were typical of future completions and commitments.

We used the C/MI commitment data on a few key variables to examine how much bias the underrepresentation of large projects

introduced into the financial data and the unit size data. Among the 12 jurisdictions in the sample with large projects uncompleted, the cost per unit started and completed appeared to differ substantially in six. Even at the end of December 1986, however, most of these projects were not completed, and it was possible that scope modifications made during construction might change the impact substantially.

A.3.4 Project and Unit Weights

While the sampling plan created largely self-weighting program-level data, the project/unit/tenant weights were more complex. The formal procedure required computing the average value at each sample site, then taking the average of the averages (with Chicago, Philadelphia, and Los Angeles data receiving extra weight). Implicitly, this procedure assumed that the number of units produced with each program dollar (or each \$5,000 program dollars) was not systematically related to grant size. An examination of C/MI completion and commitment data on rental rehab dollars per unit showed that this assumption was reasonable.

Computationally, the easiest way to apply the weights was to divide each C/MI or sample observation (of a project, owner, unit, or tenant characteristic) by the number of C/MI or sample observations at the site; further weight up the Chicago, Los Angeles, and Philadelphia data; then take the simple average of all the weighted C/MI or sample observations.

Exhibit A.11 presents the series of weights to be used in the analysis. Each is described below.

EXHIBIT A.11

Cities	(1) Weights to Generate City-wide Averages	(2) Aggregate Data/CMI Weights	(3) CMI Project Weights	(4) CMI Unit Weights	(5) Project Weights for 125 Sample Projects	(6) Unit Weights for 125 Sample Projects	(7) CMI Counts		(8) CMI Counts		(9) Sample Counts	
							No. of Projects	No. of Units	No. of Projects	No. of Units	No. of Projects	No. of Units
Chicago	2.9	1.0	0.97	.079	0.97	.079	3	37	3	37	3	37
Los Angeles	2.5	1.0	0.19	.011	0.50	.086	13	227	13	227	5	29
Philadelphia	1.3	1.0	0.65	.217	0.65	.217	2	6	2	6	2	6
Detroit	1.0	1.0	0.50	.043	0.50	.043	2	23	2	23	2	23
L.A. County	1.0	1.16	0.05	.022	0.20	.062	21	46	21	46	5	16
Houston	1.0	1.31	0.05	.025	1.00	.125	2	40	2	40	1	8
San Francisco	1.0	1.44	0.50	.200	0.50	.200	2	5	2	5	2	5
San Diego	1.0	2.02	0.10	.024	0.20	.045	10	41	10	41	5	22
Newark	1.0	2.23	0.50	.200	1.00	.500	2	5	1	2	1	2
Milwaukee	1.0	2.37	0.04	.020	0.20	.111	25	50	25	50	5	9
Cincinnati	1.0	2.52	1.00	.167	1.00	.167	1	6	1	6	1	6
Pittsburgh	1.0	2.62	0.50	.111	0.50	.111	2	9	2	9	2	9
San Antonio	1.0	2.75	0.12	.045	0.25	.056	8	10	8	10	4	5
Seattle	1.0	2.84	0.12	.045	0.20	.028	8	22	8	22	5	18
Indianapolis	1.0	3.22	0.25	.027	0.33	.028	4	37	4	37	3	36
Toledo	1.0	4.38	0.15	.083	0.25	.111	7	12	7	12	4	9
Nassau Co.	1.0	4.65	0.03	.009	0.20	.042	30	107	30	107	5	24
Birmingham	1.0	4.96	0.09	.009	0.20	.026	11	111	11	111	5	38
New Haven	1.0	5.89	0.33	.059	0.50	.091	3	17	3	17	2	11
Tulsa	1.0	6.66	0.08	.040	0.20	.125	12	25	12	25	5	8
St. Louis Co.	1.0	6.73	0.17	.111	0.33	.333	6	9	6	9	3	3
Lexington	1.0	6.87	0.09	.008	0.25	.167	11	129	11	129	5	6
Anaheim	1.0	9.00	0.10	.014	0.50	.028	10	73	10	73	5	36
St. Clair Co.	1.0	14.64	0.09	.045	0.50	.083	11	22	11	22	5	12
Anne Arundel Co.	1.0	15.70	0.20	.100	0.33	.167	5	10	5	10	3	6
Greensboro	1.0	16.17	0.33	.250	0.33	.250	3	4	3	4	3	4
Portland	1.0	16.20	0.15	.059	0.20	.083	7	17	7	17	5	12
Rockford	1.0	17.12	0.12	.056	0.25	.125	8	18	8	18	4	8
Wichita	1.0	18.68	0.06	.025	0.25	.250	16	16	16	16	4	4
Islip	1.0	20.75	0.25	.200	0.25	.200	4	5	4	5	4	4
Clackamas Co.	1.0	22.14	0.05	.014	0.20	.037	19	70	19	70	5	27
Mesa	1.0	24.83	0.15	.036	0.20	.043	7	28	7	28	5	23
Greenville	1.0	26.56	0.17	.036	0.20	.042	6	28	6	28	5	24
Alexandria	1.0	33.19	0.50	.500	0.50	.500	2	2	2	2	2	2
TOTAL	37.7						283	1,267	283	1,267	125	492

Administrative Data

The weights in Column 1 should be applied to the administrative data before averaging it to estimate how the average grant dollar was administered. On those rare occasions when a national estimate or an estimate for the average jurisdiction is needed, the weights in Column 2 should be applied to the data.

CMI Data

The sample was designed to allow accurate estimation of the characteristics of the project, unit, or tenant funded with the average grant dollar. Essentially, it was designed to describe the average project/unit/tenant once all grantees have spent the funds that they were allocated at the time of our site visit. For this forward-looking analysis, the C/MI data on projects/units/tenants should be weighted by the weights in Column 1 divided by the number of completed projects/units/tenants at the site in May 1986 as shown in Columns 7 and 8. The C/MI weights are shown in Columns 3 and 4.

Sample Projects

To profile the likely situation once all funds are expended, use the weights in Column 5, which are the weights in Column 1 divided by the number of sample projects at the site, as listed in Column 9. If each project's data are multiplied by the number of units in the project, use the weights in Column 6, which are the weights in Column 3 divided by the number of units in the sample at the site, as listed in Column 10.

Sample Units

To profile the likely situation once all funds are expended, use the weights in Column 6, which are the weights in Column 3 divided by the number of units in the sample at the site.

A.3.5 How To Use the Weights

To use the weights, multiply the data for each jurisdiction by its weight, then combine the data and divide by the sum of all the weights applied. For example, suppose two properties received weights of 0.3 and four properties received weights of 0.5. To compute the mean value per property, the data would be weighted and summed, then divided by $2 \times 0.3 + 4 \times 0.5 = 2.6$. For analyses using all the sample or C/MI data, the sum of the weights is 37.7.

When using unit-weighted project data, multiply each project observation times the number of units in the project times the unit weight for the jurisdiction (Column 4 for C/MI data and Column 6 for sample data). Sum the weighted observations and divide by the sum of the weights.

APPENDIX B

THE ACCURACY OF HUD'S C/MI DATA BASE

HUD's Cash/Management Information System (C/MI) is the primary source of data on projects developed under the Rental Rehabilitation Program. The system is designed to serve two functions. First, the C/MI collects two waves of data on each project funded under the program. A Pre-Rehab report is submitted immediately after project set-up, providing basic project data, including project and owner identifiers, estimated rehab costs, the RRP fund request, and a tenant record for each unit in the project (unit size, rent, occupancy status, tenant demographics, and assistance status). The Project Completion Report, submitted at 75% occupancy or 90 days after final draw-down, provides an equivalent post-rehab tenant record for each unit, as well as final data on rehab costs and the sources and amounts of funds used to support rehab. The data base is intended for use as an evaluation tool and also is to be used as the basis for grant adjustments based on performance criteria developed by the Department.¹ This appendix reviews the accuracy of the C/MI data.

B.1 Data Collection and Verification Procedures

For the Evaluation of the Rental Rehabilitation Program, field teams visited a sample of 35 Rental Rehab sites. Program level data

1. In addition to providing tenant and property data, the C/MI is used to control electronic fund transfers to program participants. Projects must be "set up" in the system to receive funds and permit draw downs. As an incentive for timely data submission, failure to submit required reports can trigger a hold on project funds.

were collected from interviews with city (or county) staff and with representatives of the participating PHA. At the project level, we collected data for a sample of 125 properties, based on a review of the project files, interviews with the project owner, and a physical inspection of the property.

Information on the accuracy of the C/MI comes primarily from data collection for the 125 sample projects. In each case, file and interview data were used to correct the existing C/MI data. Changes were then made to produce a corrected--and to some extent up-dated--data base. In addition, we made corrections to C/MI entries for non-sample projects wherever this was possible. However, without owner data or extensive file review, our ability to identify and correct errors for these non-sample projects was limited.

Verification for the intensive sample included the following steps. First, financial data were checked against information in the project files, including grant or loan documents, lenders' commitment letters and other program records. Financial data were then confirmed with the project owner. Tenant data, including occupancy and rent, were checked in several ways. First, program files generally contained owner applications with pre-rehab and proposed contract rents, and quite often a listing of project tenants. Second, rents and pre-and post-rehab occupancy were verified with the owner. Finally, in our interviews with PHA staff, we attempted to confirm occupancy, rents, and assistance status for the projects, as well as to identify the number and characteristics of households who moved from Rental Rehab properties during the rehab phase.

It should be pointed out that we did not attempt to independently verify individual tenant characteristics (e.g., race, income, household size, or sex of head. Such an effort would have been virtually impossible for unassisted tenants, absent tenant interviews, and extremely time consuming for other households.

B.2 Type and Frequency of Errors

Using the field procedures described above, we detected a substantial number of errors in the C/MI. Exhibit B.1 shows the percentage of errors found and corrected for a selected group of C/MI data fields. Error rates listed under "project level" fields are based on 106 sample projects for which both HUD supplied and field verified data were available. Unit level fields reflect data for 433 pre-rehab and 435 post-rehab units contained in the 106 sample projects. While error rates reflect the percentage of cases for which corrections were made¹, several caveats should be kept in mind:

- o First, in some cases changes reflect updates to the C/MI, i.e., field interviewers were able to supply missing data.
- o Second, in some cases, where data were deemed suspect and no additional information could be obtained, existing records were changed to missing.
- o Third, a single error in many cases required changes to multiple fields. For example, where data were entered for too many (or too few) units, charges are reported for each data item in the unit record.

1. Error rates for the items "RRP Funds" and "CDBG funds" reflect changes to one or more items related to this funding source, i.e., a change in the dollar amount or a change in the subsidy category. Similarly, error rates for "other funds" reflect one or more charges to data pertaining to tax exempt, other public, private loan, or other private sources of funds.

Exhibit B.1

Percentage of Errors in Selected C/MI Fields
(106 projects)

Project Level Fields:

Number of Units Pre-Rehab	8%
Number of Units Post-Rehab	6%
Owner-occupied	0%
Type of Ownership	9%
Property Type	28%
Project Involvement	16%
Total Rehabilitation Cost	28%
Rental Rehabilitation Grant Funds	7%
CDBG Funds	4%
Other Funds	19%
Total Financing Cost	14%

Unit Level Fields (Pre-Rehab):

Occupancy	8%
Number of Bedrooms	11%
Rent	46%
Tenant Income	8%
Race	9%
Household Size	7%
Sex of Head	9%
Assistance Type	7%

Unit Level Fields (Post-Rehab):

Occupancy	22%
Number of Bedrooms	15%
Rent	61%
Tenant in Project Prior to Rehab	21%
Tenant Income	16%
Race	17%
Household Size	18%
Sex of Head	19%
Assistance Type	27%

As shown in the Exhibit, project characteristic and financial data had relatively few errors, usually under 10% of the cases. One problem area was "Property Type", denoting whether the building was mixed use, a SRO, or a cooperative. These errors resulted from the failure to include an explicit category for "residential" on the input sheet, a problem of which HUD is already aware. Changes reported under "Total Cost" often included extremely minor adjustments to reflect small differences between reported rehab costs and final costs as reflected in contract documents.

Changes in the pre-rehab unit level fields were also fairly modest. The principal problem related to rents. In most cases changes resulted from a need to convert contract rents to gross rents. Although the C/MI specifies that the rent to be entered is gross rent, i.e., rent including utilities, program staff in numerous sites have apparently overlooked this instruction, and routinely entered contract rents. For pre-rehab units, a few additional changes were made for vacant units where a theoretical "market rent" had been entered.

Finally, data items related to post-rehab units show the highest error rates. Again, the most serious problem relates to rents, with changes required for 61% of the units. Other data items with a substantial number of errors are "Occupancy" and "Type of Assistance." High error rates in these categories may in part be the result of our adding missing data. Higher error rates for various tenant characteristics are most likely the result of our greater ability to catch errors for more recent tenants.

B.3 Overall Accuracy of the C/MI

Despite the substantial number of errors detected in the C/MI, the overall accuracy of the system appears to be quite good. Exhibit B.2 shows distributions and medians for selected C/MI variables drawn from the HUD supplied data tape and from the corrected version. As shown in the Exhibit, with the exception of post-rehab rents which are about 7% higher after correction, differences between the two versions are minimal. Overall, the C/MI presents a reasonably accurate picture of how the program is operating.

B.4 Improving the C/MI

HUD has already taken numerous steps to improve the accuracy of the C/MI through the issuance of new instructions to grantees and through edit and correction procedures initiated by the Department. Most importantly, the Department is working to correct the problem related to contract vs. gross rents.

It is important to point out, however, that most grantees do not view the accuracy of the C/MI as critical to their programs nor do they devote a great deal of attention to identify and/or correcting inconsistencies. In addition, to the extent that timely submission of the forms is linked to a site's ability to set up additional projects and draw down funds, the submission of incomplete, incorrect, or "missing" data can be deliberate.

While the steps HUD is currently taking should greatly improve the accuracy of the data base, some additional steps might be suggested:

1. Encourage sites to list pre- and post-rehab units in the same order. Although random order was originally suggested for privacy reasons, a one-for-one correspondence would make it

Exhibit B.2

Comparison of Original and Corrected C/MI Data ¹
 (111 Projects)

	<u>Original Data</u>	<u>Corrected Data</u>
1. Distributions of Selected Variables		
Number of Pre-Rehab Units		
1 unit	36.0%	36.9%
2-4 units	42.3%	41.4%
5-10 units	16.2%	15.3%
11-20 units	2.7%	3.6%
21+ units	2.7%	2.7%
Number of Post-Rehab Units		
1 unit	35.5%	35.1%
2-4 units	42.7%	43.2%
5-10 units	16.4%	15.3%
11-20 units	3.6%	3.6%
21+ units	1.8%	2.7%
Percent Owner Occupied	3.6%	3.6%
Ownership		
Corporation	8.1%	6.3%
Individual	71.2%	72.1%
Non-profit	0.9%	2.7%
Partnership	15.3%	15.3%
Other	4.5%	3.6%
Property Type		
Residential	56.4%	89.1%
Mixed Use	38.2%	10.9%
SRO	5.5%	0.0%

1. Data are unweighed and should be used for the purposes of comparison only. They do not reflect the experience of the national program. Data are based on 111 projects for which HUD-supplied and field-corrected data could be compared.

Exhibit B.2 (continued)

Involvement

Missing	29.7%	-
Rehab Only	63.1%	90.0%
Acquisition	5.4%	5.4%
Refinancing	1.8%	4.5%

Average Rehab Cost Per Unit

\$ 1 - \$2,500	6.3%	5.4%
\$2,501 - \$5,000	18.0%	20.7%
\$5,100 - \$7,500	10.8%	9.0%
\$7,501 - \$10,000	16.2%	18.0%
\$10,000 - \$15,000	32.4%	31.5%
Over \$15,001	16.2%	15.3%

2. Mean Values for Selected Variables

Financial Data

Total Rehab Cost	\$36,253	\$35,103
RRP Funds	13,513	13,433
CDBG Funds	38,177	36,093
Other Public Funds	9,000	12,000
Private Loan Funds	30,537	27,277
Other Private Funds	10,499	10,004
Total Financing Cost	37,493	37,530

Average Project Demographics - Pre Rehab

Percent Vacant	13.2%	11.7%
Percent Black	42.1%	40.7%
Percent Hispanic	18.5%	16.8%
Percent White	31.6%	37.6%
Percent Other	2.1%	2.0%
Percent Very Low Income	70.8%	67.9%
Percent Low Income	19.0%	17.5%
Percent Above 80% Median Income	5.4%	6.8%
Percent Elderly	14.8%	14.1%
Percent Female Headed	45.7%	46.6%
Average Rent Pre-Rehab	\$331	\$340

Exhibit B.2 (continued)

Average Project Demographics - Post Rehab

Percent Vacant	3.5%	2.5%
Percent Black	47.7%	48.0%
Percent Hispanic	13.4%	12.4%
Percent White	34.1%	32.0%
Percent Other	2.4%	2.3%
Percent Very Low Income	72.1%	70.1%
Percent Low Income	18.2%	18.3%
Percent Above 80% Median Income	7.7%	6.3%
Percent Elderly	14.3%	11.6%
Percent Female Headed	49.3%	48.9%
Average Rent Post Rehab	\$398	\$429

easier to identify inconsistencies, such as changes in bedroom count in the same unit, changes in household characteristics for a continuing family, or changes in the number of pre- and post-rehab units which are not due to unit reconfiguration.

2. Encourage sites to review the pre- and post-rehab C/MI forms for such inconsistencies prior to final submission. Presumably, errors detected through HUD's own edit checks will result in returning some forms for corrections by the grantee.
3. The sites' reliance on owners to supply tenant data is troublesome. Although this is efficient in many respects, it can lead to errors. Where grantees or PHA staff do not survey pre-rehab tenants directly, owners at a minimum might be required to collect the needed data on a form signed by the tenant in question. For post-rehab tenants complete data should be supplied by the PHA for assisted tenants, and, if at all possible, by PHA or grantee staff for unassisted tenants.
4. The pre- and post-rehab C/MI target listings provide a useful means of monitoring rehab period turnover, although they are not currently used for this purpose. Sites might be encouraged to match these listings to identify movers, and follow-up on these households as necessary.

**APPENDIX C
CATEGORIZING THE NATURE OF REPAIRS**

To provide a consistent standard for analysis purposes across all 34 sites, pre-rehab condition was rated for the following 17 systems:

- o Building exterior
- o Foundation/structure
- o Roofs and gutters
- o Auxiliary structures/site (including grading and landscaping)
- o Heating/ventilation/air conditioning (HVAC)
- o Kitchen
- o Bathroom
- o Electrical service (outside kitchens and bathrooms)
- o Plumbing (outside kitchens and bathrooms)
- o Interior common areas (halls, stairs, common rooms)
- o Interior unit surfaces
- o Windows
- o Security/safety
- o Energy conservation
- o Extermination
- o Commercial space

Unless very extensive work was done, such as rewiring of the entire unit, electrical and plumbing work related to kitchens and bathrooms were classified as part of the work on these rooms. We felt that this practice provided a better picture of the nature of improvements than classification of these problems as electrical and plumbing repairs.

We allocated the costs of rehab among the 17 systems listed above and several other categories:

- o Adaptations for the handicapped,
- o Demolition,
- o Soft costs, including the costs of financing, relocation, architecture and engineering.
- o Overhead and profit, if these were listed as a separate line item. (For analysis, this cost item was allocated proportionately among the other line items.)

We separately recorded the costs of "rehab necessary to meet local codes and/or Section 8 HQS," "other essential rehab," and "general property improvements." Many items are in the gray area between the first two categories. Among these, items that generally were classified as HQS/Code included:

- o Siding or exterior painting. This work generally is necessary to achieve weather-tightness as required by HQS. We do not believe that it would be possible or useful to identify separately those few instances in which exterior painting is done purely for cosmetic reasons. Note below, however, that painting of brick or masonry structure will be considered above HQS/Code.
- o Closets and storage areas. (HQS does have a requirement for adequate food preparation and storage space, and many local housing codes have minimum requirements for closet space in bedrooms.)
- o Bathroom and kitchen remodeling.
- o Energy conservation items, which although not technically HQS/Code items, offer such great benefits that most localities treat them as if they were HQS/Code. (Note: If new windows are being installed because of HQS/Code failure of current windows, the amounts will be recorded under the "Windows" category, rather than energy conservation.)
- o Interior painting. Interior painting will often be the result of rehabilitation (e.g., painting new wall board) or code requirements. We do not believe that it would be useful or possible to try to identify separately those limited instances in which the painting may be strictly cosmetic.

Items that generally were considered "other essential rehabilitation" (beyond HQS/Code) included:

- o Landscaping, tree trimming, mulching. However, site work to correct an erosion problem or trimming a tree that is damaging a unit would be considered HQS/Code.

- o Playgrounds, picnic areas, benches 1/ However, repair work to correct a hazard would be considered HQS/Code.
- o New fences and gates. However, repair of existing items which represent a hazard or installation of new fences/gates to correct a safety hazard would be considered HQS/Code.
- o Additional sidewalks, parking spaces. However, repairs to existing items that represent a hazard would be considered HQS/Code. Note: In some instances we have found code requirements for a specified number of spaces per unit in multifamily buildings. In these cases, additional parking spaces would be considered a code item.
- o Hosebibs/external electrical circuits (except in rare cases where this is required by code.)
- o Architectural embellishments including porches, awnings, balconies, patios. However, repairs to existing items which represent a hazard would be considered HQS/Code and lavish embellishments would be considered GPIs.
- o Accessory buildings. However, repairs to existing items which represent a hazard would be considered HQS/Code.
- o Dishwashers, compactors.
- o Installation of extra baths and half-baths, unless required by code.
- o Air conditioning installation or repair except in regions of the county in which it has been determined that air conditioning is generally provided in modest rental housing.
- o Decorative wall coverings, but lavish coverings would be considered GPIs.
- o Changing unit configurations or additions.
- o Individual utility metering.
- o Security systems, bars/grates on windows and doors.
- o Laundry room and equipment, except where required by code.

1. No expenditures actually were incurred in this category.

- o Repairs and renovation of community rooms and equipment.
- o Mailboxes, except where installation is required by the Post Office or local code.
- o Floor refinishing.

As noted above, we also obtained the costs of any general property improvements included in the scope of work.¹ When the locality classified rehab work between the HQS and other essential categories (or an eligible general property improvements category) differently than the way we categorized them, the locality's breakdown was collected as well as our standardized version. We also noted the nature of major rehab items allowed by each locality in the essential, non-HQS category.

Table C.1 lists the items classified as other essential rehab or general property improvements by the localities and our inspectors. One of the two luxury class rehabs included the only skylight and fireplace installation encountered. No wood-burning stoves or microwaves were encountered, but if they had been, they either would have been classified as GPIs or other essential rehab.

Occasionally, the rehab included items that were ineligible for rental rehab assistance. To learn if the owner made such expenditures outside the program, we asked the owner about the cost and nature of any additional work done on the property at the same time as or since the rental rehab work, as well as inspecting the property. Our rehab specialists attempted to classify which of this work was an essential response to emergent problems, which was work that our rules would

1. Since owners may be obtaining loans for the repair work, they are likely to want to include other items under a single scope. RRP sites appear to allow this, requiring the owner to fund the work with an additional contribution.

classify as essential but the city did not, and which was over and above essential rehab. Only one property had expenditures in the latter category.

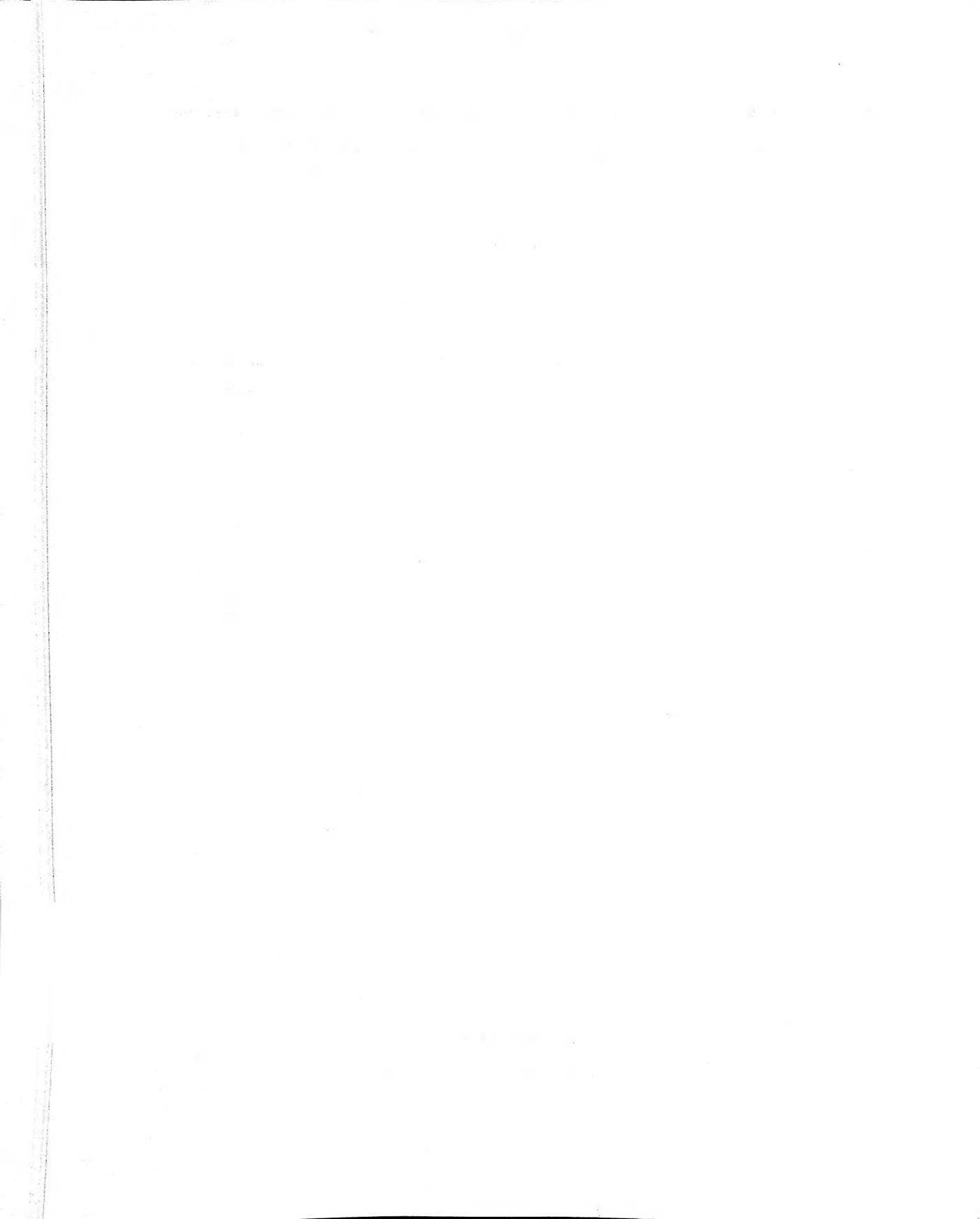
Table C.1

Other Essential and GPI Items
Identified by Local and Urban Institute Staff

<u>Item</u>	<u>Agree</u>	<u>UI Only</u>	<u>Locality Only</u>
Carpet	1	6	8
Appliances	2	5	4
Solar Water/AC	2	4 ^a	0
Energy Conservation	1	0	4
Luxury Quality	0	2 ^b	0
Landscaping	2	3	2
Fences	1	3	0
Security System	1	3	0
Exterior Surfaces	1	7	0
Downspouts	0	0	3
Porch/Garage	0	2	5
Unit Reconfiguration	1	8	0
Utility Separation	1	2	0
Miscellaneous	1	3 ^c	1

Note: Multiple items were noted at some properties.

-
- a. Two solar water heaters were coded as GPIs.
 - b. Coded as GPIs.
 - c. New commercial electric connection was coded as GPI.



APPENDIX D

**EVALUATION OF THE RENTAL
REHABILITATION PROGRAM**

NEW YORK CASE STUDY

Prepared by:

Michael Brintnall

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New York City is the largest recipient of Rental Rehabilitation program funds in the country, with a combined award of \$32 million for FY 1984 and FY 1985. New York City was selected for separate case study treatment because the program does not reflect the typical use of Rental Rehabilitation funds. Specifically, the city has not developed a new program for rental housing rehabilitation, but is instead providing supplemental funding to three existing city rental housing programs, each of which blends RRP funds with other public subsidies.

In addition to merging RRP funds into existing programs, New York City has also entered into an agreement with HUD which permits RRP funds in the largest program component to be used as take-out financing on projects that are in the process of being converted to tenant cooperatives. As a practical matter, this means that no project completion data will be available until such time as the units are transferred to private ownership. This, combined with an absence of completions in other program components, precludes an assessment of program outcomes at this time.

This case study provides an overview of the way New York City has organized and implemented its Rental Rehabilitation program, the reasons behind the program decisions it has made, its current progress, and some of the issues it has faced so far. The study is based on

interviews with New York City and HUD officials, program documents, and other available data.

D.1 The Use of RRP Funds in New York City

The New York City RRP program provides supplemental funding to three existing programs. Exhibit D.1 shows unit and dollar commitments to each, as of January 1, 1987. The following sections describe each of the three programs and the use of RRP dollars within these.

D.1.1 Participation Loan Program

The Participation Loan Program (PLP) uses Community Development Block Grant funds to provide 1% loans leveraging private funds for the rehabilitation of multi-family buildings. Private funds are loaned at market rates, and fully amortized over 15 to 30 years. Buildings included under the PLP program usually have 40 or more units and require rehabilitation involving the replacement or repair of one or more building systems and the modernization of interiors. City bond counsel has approved the substitution of city bond funds for CDBG in this program for the future.

Rental Rehabilitation funds used in the PLP are provided as 1% loans, self-amortizing over a maximum 30-year period. As of January 1, 1987, four PLP projects were underway with Rental Rehabilitation funds included, totalling 884 units and involving a commitment of \$4,633,000 in Rental Rehabilitation program funds.

D.1.2 Article 8A Loan Program

The Article 8A Loan program (8A) provides 3% loans with a maximum term of 15 years, and a maximum of \$5000 per unit, for

EXHIBIT D.1

USE OF RENTAL REHABILITATION FUNDS IN NEW YORK CITY

	<u>Participation Loan Program</u>	<u>Article 8A</u>	<u>DAMP</u>
Initial Allocation ¹	6,000,000	10,000,000	15,472,500
Dollars Committed ¹	4,633,000	5,008,233	14,464,184
Dollars Disbursed ¹	0	2,517,715	0
Dollars Final Draw ¹	0	0	0
Projects Committed ²	4	23	179
Units Committed ²	884	4,339	7,289
Average Rehab cost Per Unit (Estimated) ³	\$25,608	\$1,949	\$7,000
Subsidy Approach	Direct Loan at 1%; Maximum 30-year term.	Direct Loan at 3%; Maximum 15-year term.	Direct Loan (1% or 3%) for after sales financing/ reimbursement of CDBG funded rehab costs

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1. Source: HUD C/MI Data, December 31, 1986.
 2. Source: City Records, January 1, 1987.
 3. Source: HUD C/MI Data, June 1, 1986.

replacement of major systems in multi-family buildings in eligible community development census tracts. It is authorized by the Private Housing Finance Law of the State of New York, and is also supported with Community Block Grant funds.

In the 8A program, the city has used Rental Rehabilitation program funds both for buildings recently transferred to private ownership from city-owned stock, and for aging Mitchell-Lama housing cooperative projects. The Rental Rehabilitation money is provided as a 3% loan for a maximum of 15 years. As of January 1, 1987, 23 8A projects using RRP funds were underway, totalling 4,339 units and involving a commitment of \$5,008,233 in Rental Rehabilitation program funds.

D.1.3 DAMP

The Division of Alternative Management Programs (DAMP) physically upgrade and stabilize selected properties owned by the city through tax foreclosure (in rem properties), and return them to private ownership. Under distinct sub-programs, buildings are sold to tenant cooperatives (TIL), to non-profit community groups (CMP), or to private real estate firms with a track record in salvaging troubled projects (POMP). The program with the largest number of buildings and largest pipeline is TIL, the Tenant Interim Lease program. TIL provides organized tenant groups with an opportunity to lease, manage, and buy their city-owned buildings.

Community Development Block Grant funds (also to be replaced by city bond funds) are used in DAMP to finance rehabilitation of city-owned property before transfer to private ownership. Use of Rental

Rehabilitation program funds for this purpose has required a special waiver because there technically is no private owner until after the housing is rehabilitated and transferred from city ownership. Rental Rehabilitation program funds have been approved for use as take-out funding, to "pay back" eligible expenditures first covered by CDBG.

When Rental Rehabilitation program funds are used for after-sales support in D.A.P programs, or for the Private Ownership Management program, they are provided as loans under the terms of PLP or Section 8A. As of January 1, 1987, 179 DAMP projects were underway with Rental Rehabilitation funds included, totalling 7,289 units and involving a commitment of \$14,464,184 in Rental Rehabilitation program funds.

D.2 Program Objectives and Design

Based on New York City's long-standing commitment to rental housing rehabilitation, the initial response of city officials to the RRP was to see it as an additional resource for ongoing efforts, rather than as a new and distinct program initiative. Indeed, many housing officials in the city feel that the city's Participation Loan program (PLP) was a model for early versions of the RRP (though the final federal program design is different from many aspects of the city's approach), and it was this feeling which led to the blending of Rental Rehabilitation program funds into PLP, and into the Section 8A program.

A second factor was the high priority put on the management of the city's large stock of in rem housing. The city owns about 10,000 buildings because of tax foreclosure proceedings, and about 4,000 of these (accounting for 26,400 units as of FY 1984)¹ are occupied

1. City of New York, Department of Housing Preservation and Development, The In Rem Housing Program, Sixth Annual Report (1985), p. 43.

buildings, managed by the City of New York. The Division of Alternative Management Programs was established in 1978 to upgrade suitable buildings in this group and to transfer ownership to tenants, community groups, or private management firms. However, since the city is technically the owner of the buildings until after they are transferred to cooperatives or other owners, the city has required a waiver from HUD to use CDBG funds to rehabilitate these properties. This same technical difficulty impedes use of Rental Rehabilitation program funds in the DAMP program. Nevertheless, the DAMP program was a high enough priority for the city, and program need was deemed strong enough, that the city chose to assign a substantial share of the Rental Rehabilitation program funds to this use.¹

D.2.1 The Decision to Incorporate Rental Rehabilitation Funds into Existing Programs

In choosing to combine RRP funds into existing programs, New York City chose a distinctly different path from other grantees, which typically operated the RRP as a separate program. Program staff offer a number of reasons for doing so.

The first reason, simply, is that the other programs existed. The city was already actively engaged in efforts to rehabilitate rental

1. The city and HUD were able to agree on a procedure in which Rental Rehabilitation program funds could be committed to a building while the city owned it, but could not be drawn down until the building was in private hands. In the interim, expenditures would be covered by CDBG or city funds. In this way, RRP funds serve as a kind of take-out financing.

housing through DAMP, Section 8A, and PLP, and each of these programs had large unmet needs to which additional funds could be applied.

Second, these programs, primarily DAMP and PLP, already used CDBG funds, and thus the linkage with HUD funding and its requirements appeared relatively straightforward. While in fact it took several distinct program waivers from HUD before Rental Rehabilitation program funds could be used, in principle it appeared to the city that the blend was realistic and workable.

Third, the city wanted to "get up and running" early. Blending funds with existing programs avoided the great complexity of agreeing on a new program design, developing new staffing assignments, and the many other start-up costs of a new program approach. Though no one in the city phrased it this way, the prospect of working out a new program design within the city undoubtedly would have been a formidable task. Additionally, by merging Rental Rehabilitation funds into the ongoing programs (with existing pipelines), it was possible to commit a large amount of the initial allocation very quickly, thus earning bonus funds from HUD. In fact, it appears that some of these projects may have to be de-designated, because of program conflicts discussed below. But at the outset, it meant the city could move very quickly and in good faith to get Rental Rehabilitation program funds assigned.

Fourth, the city believed that the \$5,000 per unit RRP cap (or even the \$8,750 high-cost area limit) would not be large enough to attract matching funds and get banks to lend in low-income areas. Rather, program officials believed that a "total finance package" would be required. Although other communities have successfully relied on the

straight-match approach, New York City officials base their assessment on experience from the PLP and other programs. It also stems from what is viewed as a major city responsibility to restore and preserve the many larger multi-family buildings in the city which require a deeper subsidy than the RRP offered.

Finally, the blending of Rental Rehabilitation program funds with other programs appeared to offer the city flexibility to work around some of its internal restrictions. For example, the city budget office has limited the use of CDBG funds to no more than 50 percent of the total rehabilitation cost. This had impeded some projects undertaken in city programs. By combining Rental Rehabilitation program funds with existing city programs, it was possible to provide the deeper loans that projects required, but which were not allowed by either program alone. Similarly, the upper limits of allowed financing for Section 8A projects fell short of the lower limit for PLP projects. Rental Rehabilitation program funds added to Section 8A have permitted reaching into the gap in between.

In general, then, the decision to incorporate Rental Rehabilitation funds into existing programs emerged from a range of organizational considerations and HPD perceptions of its role and of local housing needs. While this produced a program that departs in many respects from the design of the national RRP, it nevertheless reflected an adaptation of the program in line with local perceptions of how best to preserve and expand the supply of standard, private rental stock for low income households.

D.2.2 Program Organization and Design Issues

The three city programs using Rental Rehabilitation funds are separately managed, but coordinated through the Office of Policy Analysis in the Department of Housing Preservation and Development (HPD). The coordinator develops basic program procedures, monitors HPD's compliance with RRP requirements, and serves as the liaison with HUD. The coordinator does not participate in individual building decisions or deal-making within the programs, but routinely reviews reports on projects before they are set up in HUD's C/MI system. In turn, the city program managers all appeared familiar with the Rental Rehabilitation program requirements and objectives. Vouchers and certificates for the RRP are also administered by HPD.¹

In setting up the program, the initial intention was to share Rental Rehabilitation program funds among the three recipient programs on an equal basis. However, the actual allocations were adjusted away from equal shares based on program capacity. Specifically, it became apparent early on that the DAMP program could use a larger share of the funds immediately (because it had buildings in hand for funding), and, as a result, approximately half of the RRP funds were allocated to it. The Section 8A program at the time had a stronger pipeline of projects than PLP, so it retained a one-third (32 percent) share, and the remaining funds (18 percent) were allocated to PLP.

The city also decided to request--and ultimately received--an exemption to exceed the \$5000 per unit cap established by the RRP. As a

1. Both the city's Public Housing Authority and HPD administer Section 8 programs. The RRP special allocation was assigned to HPD.

practical matter, HPD had to decide whether to reach simply the largest number of units possible, or whether to respond to deeper needs in some units with deeper subsidies. In this case, the city opted to trade off volume for depth-of-need through the high-cost exception which permits 25 percent of the funds to be used in projects with per unit grants up to \$8750. This trade off is also inherent in the city's overall approach of combining Rental Rehabilitation funds with other program funds to deepen the subsidy in almost all of its projects.

Finally, as indicated previously, property selection is driven by existing pipelines and individual program criteria. However, in compliance with RRP regulations, the city has designated 36 eligible neighborhoods in which RRP projects may be located. These neighborhoods were selected based on income, rent, and market conditions as well as the existence of concentrated public investment and upgrading already underway and the location so HPD Neighborhood Preservation Offices or HPD-funded community organizations providing similar outreach. The neighborhoods are spread throughout the city: 10 in the Bronx, 13 in Brooklyn, 7 in Manhattan, 5 in Queens, and 1 on Staten Island.

D.3 Building and Tenant Characteristics

As indicated at the outset, it is impossible to assess program outcomes for New York City, since there are no completed projects for which data are available. As of December 31, 1986, \$24 million of the \$32 million allocated in FY 1984 and FY 1985 had been committed to specific projects. While \$2.5 million had been drawn down under the 8A program to fund repairs, there were no final disbursements under any of the program components (See Exhibit D.1).

It is important to note, however, that under the DAMP program, which contains roughly half of the RRP funds, projects have initially been funded with city or CDBG funds, with RRP funds to be used for take-out financing after the properties have been converted to cooperatives. Cooperative conversion in New York City has traditionally been a legally complex and time-consuming process. As a result, this program component contains "physically complete" buildings which cannot be recorded as such until the transfer to private ownership is effected. Given the absence of post-rehab C/MI data (reported only upon completion) and difficulties accessing data from local program reporting systems (see Section D.4.1), this case study is limited to providing a general description of the types of units committed, the levels of repairs needed, and likely impacts of the program on tenants.

D.3.1 Property Conditions and Repairs

Buildings are selected for Rental Rehabilitation program funding from those available generally for the various programs. In deciding whether to use RRP funds, the program managers will consider the program's priorities as well as the needs of the individual project, after first seeing if the project is located in an eligible neighborhood. The primary consideration is whether the building needs the additional subsidy which the Rental Rehabilitation program can provide, and, in the case of the DAMP program buildings intended for tenant cooperatives, whether the tenant association is organized enough that it does not appear to be a source of possible delay.

The properties selected in New York City are typically quite large, averaging 221 units in the PLP, 189 units in the 8A program, and

41 units in the DAMP programs. This compares with an average property size of 5.9 for all committed units in the national program as of July 1986, and an average of 3.2 units in properties completed as of that date.¹ The size of the New York City projects, along with the cooperative conversion problems noted above, helps account for the lack of completions to date.

Almost all buildings scheduled to be assisted with Rental Rehabilitation program funds are occupied, but require replacement or repair of major systems. Buildings generally were built between 1900 and 1930 and may need plumbing, roof, and heating repairs as well as "a lot of plaster and patching." A typical PLP project, for example, is the following:

The building, in a mixed black and Orthodox Jewish neighborhood, was a solidly built, brick structure erected in the mid-1920's. But it had been neglected for years and was clearly headed for eventual abandonment. There had been no heat or hot water the previous winter, causing many tenants to move out. . . . The building needed a new heating and hot water system, new plumbing, new electric wiring. Its roof had holes in it and would have to be replaced. Windows leaked . . . the entire interior needed replastering and, of course, repainting.²

However, not all Rental Rehabilitation program projects require such comprehensive rehabilitation. The 8A program is designed to support rehabilitation in buildings generally housing low- and moderate-income people which do not require as extensive a renovation as addressed by the PLP program. Typically, loans will be provided to replace one or

1. See The Third Annual Report to Congress on the Rental Rehabilitation Program, HUD, September 1986.

2. This project is described in the 1985 Annual Report of the New York City Community Preservation Corporation. This particular project was undertaken with PLP funds before the Rental Rehabilitation program was available, and did not use Rental Rehabilitation program funds.

two capital items: thermal replacement windows, new boilers, elevator upgrading, etc.

The city has also used Rental Rehabilitation program funds to add two types of buildings to this program: 1) buildings under court-appointed administration with tenant groups in place who have expressed a capability to manage the building, and 2) aging Mitchell-Lama projects, which are large cooperatives (often involving several high-rise structures with many units). In the former case, called the Ownership Transfer Program, projects average about \$2500 per dwelling unit of Rental Rehabilitation program funds. In the case of Mitchell-Lama, repairs to a typical RRP project have included reroofing, new lobby doors in one building, and a new boiler. There are 2700 units altogether in this Mitchell-Lama project, receiving \$1.8 million in Rental Rehabilitation program funds, for a modest grant per unit of \$650. No vouchers or certificates are used in these buildings.

Exhibit D.1 shows estimated per unit rehabilitation costs for each component of the program, based on units committed as of June, 1986.¹ As shown, total rehabilitation costs for Article 8A projects should be on the order of \$1,949 per unit. PLP projects will be considerable more expensive (\$25,608 per unit), although these account for only 18 percent of the total allocation. Rehabilitation costs for DAMP--the largest single component--should be about \$7000 per unit. The

1. Note that these data are somewhat dated and include only about half of the units currently committed under each program component. Nevertheless, they provide a reasonable basis for looking at estimated rehab costs.

average unit in the national RRP program cost about \$10,000 to rehabilitate.

D.3.2 Tenant Characteristics and Tenant Assistance Policies

Currently, 75 percent of tenants in committed projects are lower income, that is, with incomes at or below 80 percent of median. The DAMP projects in particular contain lower income tenants, 84 percent of whom have incomes under 80 percent of area median. Except under exceptional circumstances, the RRP requires grantees to meet a 70 percent lower income benefit standard. Assuming that post-rehab tenant characteristics are not significantly different from those for pre-rehab tenants, the program is meeting the approved 70 percent standard.

Virtually all buildings rehabilitated by the city using Rental Rehabilitation program funds are occupied, and renovation rarely alters the number or configuration of apartments. Rehabilitation is usually performed with tenants in place, and moves will be made within the building if a unit must temporarily be vacated for repair. The city, thus, expects little displacement under the program, and no appreciable number of vouchers and certificates are expected to be used for this purpose. The city currently operates under a formal displacement policy developed for other community development programs, and not specifically tailored to the Rental Rehabilitation program.

Nevertheless, there are some circumstances in which displacement may occur in the city's program for which a more precisely tailored displacement policy may need to be developed. These circumstances include: (1) the few vacant buildings the program has rehabilitated (or may rehabilitate in the future) from which tenants may have been dis-

placed at some earlier time; and (2) tenants who find they qualify for rental assistance, but are presently in a unit with too few bedrooms. The city is aware of these contingencies, but has not planned formally for a response when they might occur.

City staff also believe that very few households have moved from the units to date, i.e., voluntarily left the buildings because of the rehabilitation activity or its effect on future rents. Like most other programs, New York City does not explicitly monitor tenant turnover. While, nationally, 28 percent of all pre-rehab households moved from the RRP properties prior to completion, managers familiar with the New York City projects all said that movers are infrequent, due to the tight rental market in the city and the fact that rents remain stabilized in the rehabilitated buildings.

To date, no vouchers and certificates have been issued in connection with the program, because appropriate buildings are not yet complete. However, income verification efforts have begun in some sites. The city also has not issued vouchers or certificates for interim use, apparently because there is already an adequate supply in their other programs. As in other city RRP programs, there appears to be some tendency to favor the use of Section 8 vouchers over certificates, primarily because of greater familiarity with the certificates. In addition, some community groups have apparently persuaded tenants that certificates are "better than vouchers" because of their 15 years of budget authority.

Nevertheless, the city does face a major issue related to the use of vouchers, since HUD permits only 5 percent of the vouchers in a

PHA to be used in cooperative buildings. Since a large share of the DAMP projects will be sold to tenant cooperatives, this restriction poses an obstacle to the New York program, and the city is seeking legislative relief from this limitation. For those cooperative buildings already committed, there are currently enough certificates to meet tenant needs. If additional cooperatives are committed, however, some solution will have to be found. One suggestion has been that the city seek approval to swap RRP vouchers for certificates to meet these needs.

D.3.3 Rent Levels and Affordability

New York City controls rents in two ways.¹ Rent "control" applies to units in buildings built before 1947 with continuous, same-family occupancy since 1971, and strictly limits rent increases. Rent "stabilization" applies to all buildings built after 1947, and to all units with turnover among tenants since 1971; under "stabilization", rent increases are allowed to reflect actual project costs. Following rehabilitation, under each of the three RRP program components, rents in all units will be restructured to the level required to recover the costs of rehabilitation and to permit sound management and maintenance.

Rehabilitation does cause rents to go up. Under the PLP program, for example, typical pre-rehab rents are \$45 per room (\$135 for a one-bedroom apartment) in controlled units, and \$63 per room (\$189) in stabilized units. Rehabilitation under PLP is likely to increase this

1. The RRP preempts state or local rent controls except where controls are maintained pursuant to a state or local ordinance of general applicability in effect prior to November 30, 1983. New York City has operated under rent control since World War II.

to \$80 per room (\$240 for a one-bedroom)--still a relatively affordable level, though still also requiring rental assistance for many families.

In the Section 8A program, rents in a Mitchell-Lama project (which typically involve more limited repairs than the PLP or DAMP buildings) will increase by 15 percent. In these projects, however, the cooperative is funding its share of the rehabilitation on a pay-as-you-go basis, and the rent increase will thus result in a surplus over strict rehabilitation costs when the work is complete and full payback is covered.

In the DAMP program, with city-owned in rem buildings, rents go through a similar restructuring, in two stages. When the city initially acquires the building, rents are restructured on an interim basis, usually at about \$35. to \$45 per room. These rents are lower than rents will be after conversion to private ownership, in part because the city has lower costs (e.g., taxes and insurance). At the point of private sale, operating budgets for the building under private ownership will be calculated, and rents restructured to an appropriate level. Typical rents after conversion are expected to be \$50 to \$65 per room, with an average unit containing 4.5 rooms.

While under rent stabilization, final rents will remain quite modest, rental supplements will nevertheless be required for the units to remain affordable to many lower income households. In most of the projects rehabilitated with RRP funds, the availability of certificates and vouchers is considered essential.

D.4 Program Administration and Management

The three city programs using Rental Rehabilitation program funds are coordinated through the Office of Policy Analysis in HPD. The coordinator oversees program operations, which are implemented directly by managers in each of the three program components. The following sections describe procedures developed to date for implementing RRP-funded activities.

D.4.1 Tracking

An automated system for tracking Rental Rehabilitation projects in the city still is not complete. A computer tracking system has been designed, and key forms and procedures have been developed for data entry. To date, however, record keeping and tabulation are still done manually.

The manual system is based on a Rental Rehabilitation Tracking Form devised by the city. This form is filled out at the time of project set-up and submitted to the program coordinator. The HUD field office monitoring reports indicate that this has been done regularly and accurately. The form provides key information about each project, including Rental Rehabilitation program funds per unit, units by bedroom size, displacement, neighborhood eligibility, and other policy information. The data is then updated manually in the program coordinators' files with information from the program offices and the city fiscal office regarding drawdowns, requisitions, and completions.

In general, development of specific tracking systems for the Rental Rehabilitation program has lagged behind actual operation of the program. This undoubtedly is a consequence of the city's decision to

integrate Rental Rehabilitation program funds into existing city operations, which permitted moving ahead quickly by relying on existing records systems for each of the programs. The HUD field office has been in active discussion with HPD regarding development of specific tracking and record keeping systems for the Rental Rehabilitation program.

D.4.2 Scope of Work and Construction Monitoring

The scope of work for rehabilitation, and the monitoring of construction progress and completion under that scope of work, are carried out individually by the three city programs, using their existing staff and procedures. There are separate management oversight divisions for each program. For example, in the PLP program, the Bureau of Engineering and Architecture will oversee the proposed scope of work. This Bureau reports to the same Deputy Commissioner, heading the Office of Development, as the Division arranging the financing for the deals. On a day-to-day basis, the project must have a supervisory engineer, paid for by the borrower, hired by the bank, and approved by HPD. The project must meet local building codes and Section 8 Housing Quality Standards as determined by the Engineering and Architecture staff.

In the Section 8A program, work is overseen by the Engineering and Cost Analysis Unit which reports in parallel with the 8A loan processing unit to the Director of Operations, who reports in turn to a second Deputy Commissioner. The DAMP program reports to a third Deputy Commissioner. This office also includes its own staff for technical support in reviewing building reconstruction. For actual construction work, in some program areas, DAMP has recently used construction

management contracts to provide technical rehabilitation services. Prior to this, the city bid out construction work building by building, which proved excessively time consuming.

D.4.3 Funds Drawdown

Rather than draw Rental Rehabilitation program funds directly through HUD's Cash Management Information system (C/MI), the city has established its own "lump-sum" drawdown system for paying rehabilitation vendors. City tax levy funds are allocated to three separate budget codes, one for each program using Rental Rehabilitation program funds, and a separate interest-bearing bank account has been established for each. Periodically, city funds are drawn down into these bank accounts. Payments for rehabilitation work on approved projects are then made from the accounts, after engineering inspections to verify the work is satisfactorily completed.

On a monthly basis, the city requisitions Rental Rehabilitation program funds to reimburse the city for the eligible expenses made from the city account. (For in rem buildings in the DAMP program, the requisition of Rental Rehabilitation program funds is not made until the building enters private hands.) The system requires a subsidiary set of accounting books to keep a record of the interim transactions in which funds eligible for payment by the Rental Rehabilitation program are initially paid out of city funds. It also causes the city to bear the borrowing costs of program funds for up to a month before HUD reimbursement. The reason behind this two-step payment system was apparently a concern on the part of HPD program managers that banks would not trust the C/MI system.

D.4.4 Administrative Costs

Most administrative costs of the Rental Rehabilitation program have been absorbed within existing program structures. Each program has added at least one staff member since undertaking the Rental Rehabilitation program work, though staff are not assigned exclusively to work on the RRP.

D.5 Program Performance

HUD has established a set of six program performance measures for the RRP, including measures based on commitment and completion rates, leveraging ratio and size of the public subsidy, the percentages of two and three bedroom units produced, affordability of the completed units, and proportion of pre-rehab tenants served. In the absence of post-rehab C/MI data, outcomes related to these performance criteria cannot yet be assessed. Therefore, the following sections provide a general discussion of the city's performance to date, problems encountered or expected, and tradeoffs involved in program operations.

D.5.1 Meeting HUD Performance Criteria

One of the possible dilemmas of splitting Rental Rehabilitation program funds among three separate programs is coordinating efforts to meet HUD performance criteria. So far, New York City has not faced difficulties in this way, however. Indeed, at the outset, the availability of three ongoing programs has probably worked to the city's advantage, since it was possible to allocate funds promptly to programs with feasible projects, and thus to commit a large proportion of the RRP allocation quickly. One-third of FY 1984 and FY 1985 funds were

committed by the end of FY 1985, resulting in HUD's decision to provide the City with an additional \$500,000 in RRP funding.

Meeting other performance criteria, such as leveraging, emphasizing large bedroom units, keeping rents affordable, etc., are guided more by the structure of the available housing stock and the character of the existing programs than explicit policy decisions or coordination techniques. The one area in which the city has had problems is in emphasizing large units. As in other sites, particularly larger cities, the requirement that 70 percent of all units contain two or more bedrooms has apparently been difficult to maintain. Difficulties in meeting guidelines for large units, according to the city staff, stem from characteristics of the city housing stock itself. For example, in its application, the city cited experience with stock included in its Section 8 Moderate Rehabilitation program showing only 55 percent of the units as having two or more bedrooms. However, the city's request for a waiver of the 70 percent requirement was not approved by HUD. Current experience in the DAMP program is 60 percent for units with two or more bedrooms and 26 percent for units with three or more bedrooms.

While the city meets HUD's lower income benefit standard (70 percent) overall, there are some variations among programs. For example, in the Mitchell-Lama projects rehabilitated under the 8A less than 70 percent of the tenants are lower income. The city considers these important buildings to include in the program, however, and is able to counterbalance the low proportion of lower income tenants in these projects with other projects (e.g., DAMP) which have much higher

proportions of lower income tenants. As indicated previously, the overall proportion of lower income tenants is about 75 percent.

Probably the greatest performance challenge for the city will be program completion, especially in the component of the DAMP program which seeks to convert the rehabilitated buildings to tenant cooperative ownership. The legal technicalities in establishing private ownership in this case are exceedingly complex and can take several years. As a result, though the city has completed the physical rehab of numerous buildings under this component, a formal completion cannot be recorded until the transfer of ownership is effected.

D.5.2 Program Conflicts and Problems

The unique use of RRP funds in New York City has led to some unique problems. One area in which the city is concerned about possible conflicts between its operations and Rental Rehabilitation Program requirements, at least for some buildings, is in demonstrating that all units meet Section 8 Housing Quality Standards after rehabilitation. Specifically, in some DAMP projects, public funds are being used to repair basic building systems, but tenants themselves are contributing "sweat equity" by completing some of the remaining repairs such as plastering or painting. At the same time, the city does not have the staff to inspect all tenant-performed repairs. Thus, while the city has arranged for rehabilitation work to meet Section 8 Housing Quality Standards, and is confident that it does, it has not formally inspected all units for compliance. If such buildings are sold to the tenants, the city is concerned that there could be a risk of legal action against the tenant cooperative for failing to comply with RRP requirements.

Since the city does not want to place this risk on the tenant cooperatives, it may be forced to "de-commit" these projects. In the future, selection of buildings to receive RRP assistance will attempt to avoid this situation.

Another problem within the program has been delay. In addition to some delay associated with start up--e.g., negotiating waivers--there have also been delays in individual projects, which city program staff and private lenders attributed most often to prolonged legal processing within the city bureaucracy e.g., getting sales documents approved, settling on appropriate wording, and passing through multiple clearances. The procedural cautiousness which affects the program appears to stem from a relatively turbulent environment surrounding previous subsidized housing activities by the city.

Legal challenges, for example, froze the city rent restructuring process in DAMP buildings from late 1982 through spring 1984. The process of converting city-owned buildings to cooperatives was stalled for three years before agreements were reached which would preclude possible windfall profits to the new owners of in rem buildings caused by gentrification of areas in which they acquired their buildings.¹ These issues are resolved and buildings are now being sold to cooperatives. Nevertheless, they have apparently contributed to a climate of legal cautiousness which many in the city suggest is delaying projects.

1. Under the solution to this conflict, after acquiring tenant acquires ownership of his or her unit in an in rem building, if the unit is sold within 25 years, and is appraised at greater than \$2500, the seller must return 40 percent of the capital gain to the city.

Another area of potential delay the city will be facing is actual construction completion. Too few projects are fully underway at this time to establish a city track record in completion of projects with Rental Rehabilitation Program funds. Nevertheless, timely construction completion is an issue which HUD officials familiar with the New York situation believe will be one of the greatest challenges the city program will face.

D.5.3 Overall Assessment and Future Directions

As of January 1987, the New York City RRP program had committed roughly 75 percent of the funds allocated to it in FY 1984 and 1985. This relatively high commitment rate results in large part from the city's decision to use RRP funds to supplement three existing city programs. The way RRP funds have been used in New York City reflects a local adaptation of the RRP to meet locally defined needs, but also produces a program that deviates from the basic RRP model.

Specifically:

- o Unlike most grantees, the city has not created a new, administratively distinct program.
- o As a result, existing program guidelines drive many design features -- e.g., property selection criteria.
- o The program is funding a substantial proportion of cooperatives, which play a small role in the RRP as a whole.
- o The fact that many properties are currently city-owned means that RRP funds will be used for after sales financing or to reimburse the city for CD funded repairs.

As a result of these decisions, program outcomes in New York will differ from those in other sites in two major ways.

First, projects rehabilitated under the New York City RRP will be much larger than those rehabilitated through the RRP generally. Although many grantees (particularly larger cities) have committed a few large projects, the majority of New York City projects contain upwards of 40 units, and some contain over a thousand units. Second, virtually all of the New York City projects will receive additional public funding, and few will operate on a straight RRP/private owner match. Again, other sites have committed additional public funds to some of their projects; nevertheless, the majority of units, nationally, receive subsidies solely through the RRP program.

At the present time, New York City is exploring the possibility of using some RRP funds in a program aimed at smaller rental properties requiring a shallower subsidy, and using only RRP funds, most likely offered as a grant. This would be closer to the conventional use of RRP funds. Nevertheless, if the city does proceed in this direction it would still be likely to follow its established practice of making this activity a component of an existing program, such as PLP, as opposed to a stand-alone RRP initiative.

Despite the differences between the New York experience and other sites, the program, as it operates in New York City, is nevertheless proceeding as expected. Based on the incomes of current tenants (pending completion reports) the program is serving lower income tenants, with 75 percent of all households having incomes less than 80 percent of area median. Although units being rehabilitated through PLP have estimated per unit rehab costs of approximately \$25,000, those under Section 8A have very low rehabilitation costs, and units under

DAMP (accounting for about half of the program funds) fall into the moderate range, with average rehab costs of \$7,000 per unit. Based on proposed rents, the units should be affordable, renting at or below the FMR.

Although data are not available to estimate leveraging ratios or total public costs, these can be expected to deviate from the national program due to the frequent use of additional subsidy and the absence of any private funds in some projects. New York also appears to have had some difficulty in meeting the 70 percent large unit requirements, though this has also been difficult for some other sites. At this time, an estimated 60% of the units contain two or more bedrooms.

The area of program performance that warrants close monitoring -- according to local observers -- is the ability of the New York City program to complete projects in a timely manner. Both the size of the projects and the unique arrangements made for city-owned properties suggest that completions will be slow. Nevertheless, the city's ability to oversee construction activity and finish projects as rapidly as possible will be an important factor in the program's ultimate performance.

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