

DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

HOUSING

FHA--GENERAL AND SPECIAL RISK INSURANCE

PROGRAM PERFORMANCE

STRATEGIC GOAL/OBJECTIVE	ACTUAL 2002	ESTIMATE 2003	ESTIMATE 2004
Strategic Goal A: Promote decent affordable housing.			
Discretionary BA (Dollars in Thousands)	\$271,617	\$229,099	\$231,771
FTE			
Headquarters	161	194	194
Field	651	602	598
Subtotal	812	796	792
S&E Cost (Dollars in Thousands)			
Personal Services	\$67,284	\$68,236	\$69,739
Travel	996	809	845
Transportation of Things	0	0	0
Rent, Communications & Utilities	0	0	0
Printing	108	166	168
Other Services	150	88	64
Supplies	53	52	52
Furniture & Equipment	0	0	0
Claims & Indemnities	0	0	0
Subtotal	68,591	69,351	70,868
Strategic Objective A.1: Expand access to affordable rental housing.			
Indicator: FHA endorses at least 800 multifamily mortgages.	1,104	800	800
Indicator: Under the Mark-to-Market program (M2M), HUD will reduce the rents and, where appropriate, complete a mortgage restructuring on 380 deals.	510	500	380

EXPLANATION OF PERFORMANCE

Performance/Means and Strategies

Funding in the amount of \$231.8 million in program funding and \$70.9 million in Salaries and Expenses for a total of \$302.6 million to support Strategic Goal A: Promote decent affordable housing.

GI/SRI Insurance Programs. The Department will continue to offer a range of alternative loan guarantee programs to address specialized mortgage financing needs. These products include mortgage insurance for rehabilitating, developing, and refinancing of apartment buildings,

nursing home facilities, nonprofit hospitals and Title I loans. The Department's insurance programs will continue to meet the Nation's need for decent, safe and affordable housing.

Multifamily Credit Subsidy Rates. The Department continuously devotes significant efforts in updating and refining credit subsidy estimates. The credit subsidy estimates were developed after extensive consultation with OMB by FHA and reflect substantial additional analysis by the Department. Each year the extensive statistical base, from which projections of future loan performance is calculated, is updated for an additional year of actual data. The Department and the Office of Management and Budget (OMB) continue to examine the data, assumptions, and calculations, which are used to estimate loan program cash flows and subsidy rates in order to eliminate errors, and to seek improvements in the accuracy and reliability of the analysis.

The multifamily credit subsidy rates used in previous years reflected historic performance data for similar loans made over the past 40 years. Concerns were raised over the accuracy of these assumptions based on historical data in light of recent improvements in underwriting, program monitoring, and asset management, as well as unprecedented changes in tax law in the 1980's adversely affecting the performance of loans in the FHA portfolio at that time.

In the fiscal year 2003 Budget, the Department and OMB agreed to change the methodology used to calculate new construction conditional claim and prepayment rates for credit subsidy rate estimates through the application of new econometric analyses applied to loan level data. For the fiscal year 2004 Budget, updated loan performance data combined with the improvement of the recovery lag calculations in the cash flow model itself yield a break-even premium at 50 basis points for the section 221(d)(4) program that serves as the primary apartment development program of FHA. This is a seven basis point reduction in the premium in effect for the current fiscal year. In addition, FHA will reduce the premium for section 207 manufactured home parks and section 220 development loans to 50 basis points, which is an 11 basis point reduction. This is also a break-even premium rate for this risk category requiring no appropriated credit subsidy. Positive credit subsidy continues to be required for the section 221(d)(3), 223(d) and 241(a) loan programs so no reduction in the applicable 80 basis point insurance premiums is proposed.

Title I Program Subsidy Rates. The fiscal year 2004 estimates for the Title I Programs reflect the loan characteristics of the property improvement and the manufactured housing program, which are incorporated into the cash flows used to calculate the subsidy rate for loan programs, in accordance with the Federal Credit Reform Act of 1990.

Title II Program Single Family Subsidy Rates. The GI/SRI single family credit subsidy estimates also reflect review of loan performance. This includes updated loan performance data and assumptions of the major GI/SRI single-family programs that are currently active. Those mortgage insurance programs are 234(c) Condominium Housing and 203(k) Purchase/Rehabilitation. Premium policy changes for the 203(k) program in the 2004 Budget include cancellation of annual premium when loan to value reaches 65 percent, rather than 78 percent. On an average 203(k) loan, it is estimated that annual premium will be required for the first 17 years of a 30-year term. With this slight alteration of the premium structure, this program is expected to break even and require no positive credit subsidy appropriations. Other small programs that do not have sufficient volume to model and estimate individually are included in the Section 234(c) risk category for budgetary purposes.

Office of Multifamily Housing Assistance Restructuring (OMHAR). The Multifamily Assisted Housing Reform and Affordability Act of 1997 was included in the 1998 Appropriations Act. The initial legislative authority establishing OMHAR ended September 30, 2001. Prior to expiration, Public Law 107-116 extended OMHAR as an entity within the Office of Housing for an additional 3 years through fiscal year 2004 and extended the attendant mortgage restructuring authorities for another 5 years through fiscal year 2006. The restructuring process is expected to preserve over 174,000 units of affordable housing stock through long-term use agreements.

The restructurings are performed through oversight of a national network of 13 public Participating Administrative Entities (PAEs), and 8 private partners. OMHAR staff is currently located in a central District of Columbia office and three satellite field offices, located in Chicago, New York and San Francisco, which oversees the program through nationally consistent guidelines, which provide for local flexibility to the extent possible.

As of December 1, 2002, OMHAR reported completing over 1,600 restructurings, averaging 35-40 per month, and resulting in an annual reduction of Section 8 outlays of \$115,096,455. The average rent reduction is \$93 per unit per month. The reductions in future Section 8 outlays and expected recoveries of second mortgage payments exceed the one-time costs of restructuring for FHA claims and PAE costs. In addition to ensuring long-term financial viability and achieving Section 8 savings, physical and managerial assessments are conducted for each property to assure the long-term viability of the portfolio. Expenses are analyzed to ensure efficient operations. Immediate capital needs are addressed through repair escrows. Long-term physical needs are provided for through increased deposits to reserve for replacement accounts. Initial deposits to

these accounts were increased on average from \$1,343 to \$2,329 per unit, and annual deposits increased on average from \$297 to \$439 per unit per year.

The M2M program realigns the owners' and HUD's interest by providing a return on the owner's equity through a capital recovery payment, an incentive performance fee, and 25 percent of net cash flow. The financial structure of the properties is designed to ensure efficient operations and maintenance of the properties. HUD is closely monitoring the performance of restructured properties through a portfolio management contract and through a "watch list" for at-risk properties which had rents reduced without a debt restructuring.

A significant amount of work still remains to be completed. Over 600 deals are currently in various stages of restructuring. There are another 2,600 Section 8 contracts expiring through fiscal year 2006, at least a third of which are estimated to be above market and eligible for M2M.

Multifamily Enforcement. The Department's multifamily housing enforcement strategy reflects the integrated and coordinated efforts of the Real Estate Assessment Center (REAC) within the Office of Public and Indian Housing and the Departmental Enforcement Center (DEC), an element of the Office of the General Counsel. REAC is completing a comprehensive and uniform portfolio wide assessment of the physical and financial condition of all the properties. Results are being forwarded to Housing's Multifamily Hubs for additional actions. The Multifamily Hubs are responsible for servicing the loans and overseeing subsidy contracts. In those cases where there appear to be severe performance problems, cases are referred to the DEC. The DEC evaluates each case it receives and, where the DEC decides that severe problems exist, the DEC provides an action plan to be implemented by the Hubs to address the problem(s). Qualitative improvement in the assessment and enforcement effort is being realized through the centralization and specialization of these staff. The ultimate goal, however, is improved living conditions for residents, improved neighborhoods, communities, and improved financial performance for FHA because performance standards for participants are raised.

HUD strongly believes in the importance of improving the management accountability of public and assisted housing programs. Housing agencies and multifamily project owners have an obligation to both the families they serve and the American people: to provide quality housing, at reasonable costs, to as many households as possible within available funding.

HUD is committed to improving the quality of HUD-assisted housing, with the goal of ensuring that all subsidized families live in units that meet basic quality standards. HUD will utilize increased oversight; management rating systems and sanctions to substantially reduce the share of subsidized housing that is sub-standard.

Resource Management Information

Discretionary BA is expected to increase for fiscal year 2004 from fiscal year 2003, based on GI/SRI program account increase between these years. Staffing decreases slightly from fiscal year 2003 to 2004 to realign FTE based on Departmental programmatic priorities.