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The Long-Term Costs of Lower-Income Housing Assistance Programs

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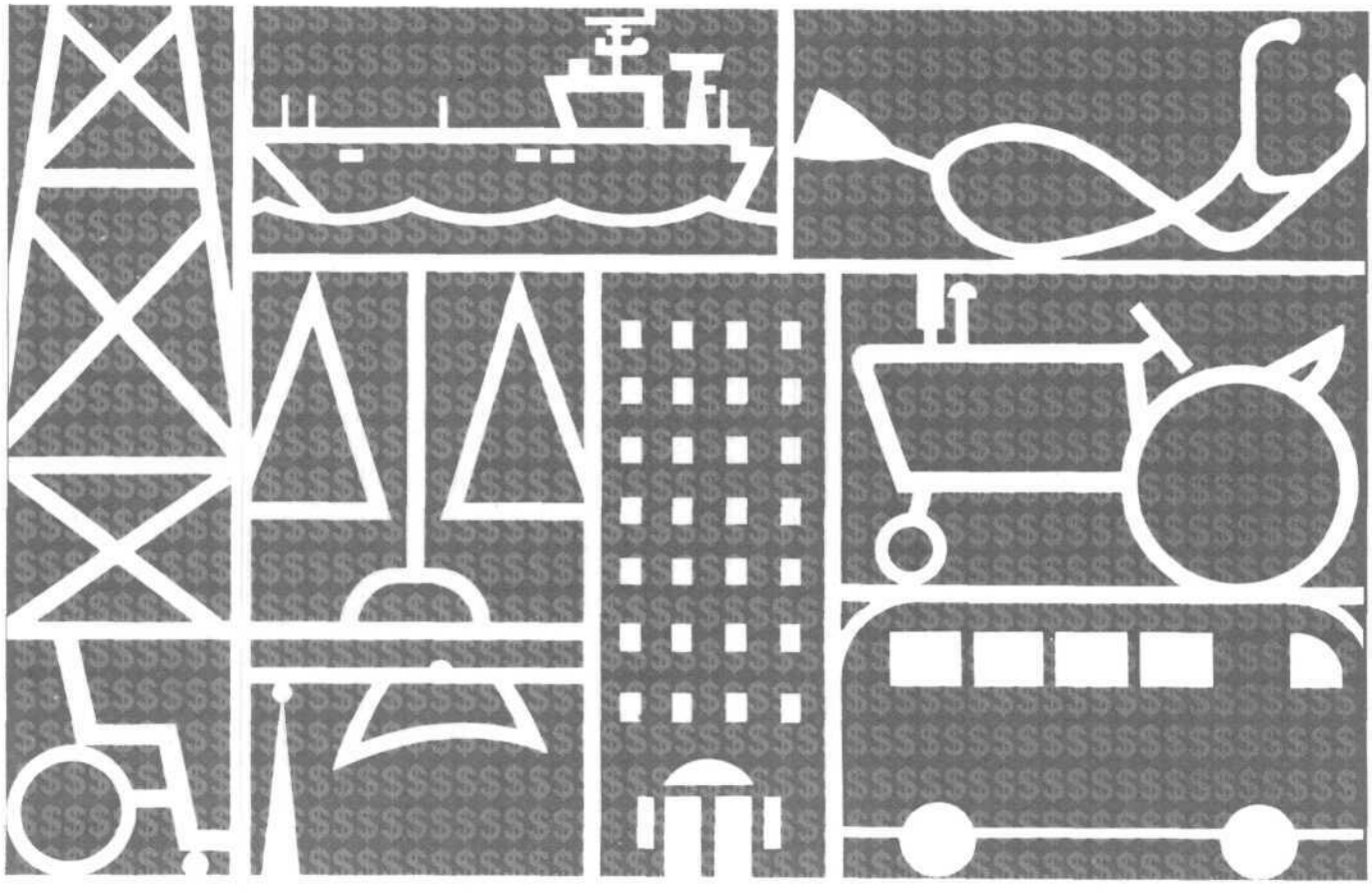

Congressional Budget Office
Congress of the United States

THE LONG-TERM COSTS OF LOWER-INCOME HOUSING ASSISTANCE PROGRAMS

The Congress of the United States

Congressional Budget Office

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PREFACE

Each year, the Congress faces important decisions concerning the funding of housing assistance programs. These decisions are made more difficult by the complex procedures used to finance housing assistance and by uncertainty regarding program costs. This paper, prepared at the request of the Senate Budget Committee, describes current funding procedures and presents estimates of the long-term costs of lower-income housing assistance programs. Alternative budgetary treatments for housing assistance programs and options for reducing long-term costs are also examined.

Martin D. Levine of CBO's Human Resources and Community Development Division prepared this paper under the supervision of Robert D. Reischauer and David S. Mundel. Fay Jan Lim developed the computer models used to estimate long-term program costs and carried out most of the data analysis. Lorene Yap and Jack Goodman of The Urban Institute assisted in developing the methodologies for preparing the cost estimates. Robert H. Kuehn, Jr. prepared the estimates of real estate tax shelter costs and provided useful comments on earlier drafts of the paper. Allan Mandel, Robert Fulton, Rodger Schlickeisen, and Don Campbell of the Senate Budget Committee staff and members of the staffs of several other Congressional committees provided helpful comments throughout the preparation of the paper. Numerous members of the CBO staff also contributed useful comments. Many persons at the U.S. Department of Housing and Urban Development provided program data upon which the cost estimates are based. Patricia H. Johnston edited the paper. Jill Bury expertly typed the several drafts and prepared the manuscript for publication.

In accordance with CBO's mandate to provide objective and impartial analysis, this paper contains no recommendations.

Alice M. Rivlin
Director

March 1979

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SUMMARY

Federal programs that provide housing assistance for lower-income families present the Congress with difficult budgetary considerations. Since these programs involve 15- to 40-year federal obligations for each unit of subsidized housing, an amount of budget authority is set aside at the time a commitment is made to pay at least a portion of the long-term direct costs. The procedures used to determine the amount of budget authority to be provided, however, do not consider all of the factors that will affect eventual expenditures. Also, there are some direct expenses and indirect subsidy costs that are not explicitly considered when new commitments are made. Thus:

- The Congress cannot be confident that the amount of budget authority initially reserved will be adequate and that additional spending authority will not be needed in the future to meet the obligation; and

- There is no way to determine from current budget documents either the total cost of different housing assistance programs or how those costs compare with nonhousing programs that are not funded in advance.

CURRENT FUNDING PROCEDURES FOR HOUSING ASSISTANCE PROGRAMS

The Section 8 Existing Housing Program 1/

The Section 8 existing housing program subsidizes lower-income persons living in existing, private rental housing. Under this program, HUD provides funds to state and local housing agencies that, in turn, make payments to landlords on behalf of persons living in units that satisfy minimum quality standards and rent for less than government-established maximums. Tenants pay between 15 and 25 percent of their incomes toward their own housing expenses and HUD payments cover the remainder.

1/ Section 8 of the United States Housing Act of 1937, as amended by the Housing and Community Development Act of 1974 (P.L. 93-383).

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When HUD enters into a Section 8 existing housing assistance agreement, an amount of budget authority is set aside to cover the assistance payments for the full 15-year term of the contract. In calculating the amount of budget authority, HUD currently considers only the amount of the first-year rent and the length of the subsidy commitment. Actual long-term costs, however, will depend not only on starting rent levels, but also on initial tenant incomes, the shares of income that tenants contribute toward rent, and the rates by which rents and tenant incomes change over time.

The Section 8 New Construction/ Substantial Rehabilitation Program

The Section 8 new construction/substantial rehabilitation program subsidizes persons living in newly built or extensively rebuilt housing. Under this program, HUD contracts with private developers prior to the start of construction to make assistance payments on behalf of lower-income tenants for a period of up to 40 years following completion of the project. When a new assistance commitment is made by HUD, an amount of budget authority is reserved to pay the difference between the tenant's contribution of 15 to 25 percent of income and the market rents for the housing for the full term of the agreement. As with the Section 8 existing housing program, the procedure used to determine the amount of funds to be set aside considers only the initial rent and the length of the commitment. Actual costs will depend on the same factors that affect multiyear costs in the existing housing program.

Current budget documents do not consider many indirect costs of the Section 8 new construction/substantial rehabilitation program. Indirect costs include mortgage-interest subsidies for private developers, foregone federal tax revenues from tax-exempt bonds issued by public housing agencies to finance certain projects, and tax expenditures resulting from favorable tax treatments that are available only to investors in subsidized rental housing.

The Public Housing Program

Under the public housing program, HUD pays the full construction and financing expenses and a share of the ongoing

operating costs for projects that are developed and owned by state and local agencies and rented to lower-income tenants. Public housing projects are financed through tax-exempt bonds and notes issued by the local agencies. At the time that HUD makes an assistance commitment, an amount of budget authority is reserved to pay the principal and interest costs on the public indebtedness in 40 equal annual installments. The annual operating subsidies that are paid to local agencies to reduce tenant rent payments to levels slightly lower than those in Section 8 are not financed in advance but are funded, instead, through annual appropriations. Long-term revenue losses resulting from the tax-exempt bond financing are also not shown in the budget when new public housing commitments are made.

PROJECTED PROGRAM COSTS

Total Long-Term Costs in Comparison to the Amount of Budget Authority Available

The long-term costs of all housing assistance programs depend on the rates of increase in housing expenses and tenant incomes over an extended period of time. Even under fairly optimistic assumptions concerning future increases in rents and tenant incomes, direct subsidy costs are likely to exceed the amount of funds reserved under the Section 8 programs, especially for the lengthier new construction/substantial rehabilitation commitments (see Table S-1). Because funds are not provided at the outset to pay operating subsidies, the long-term direct subsidy costs of the public housing program consistently exceed the amount of budget authority reserved. When indirect expenditures are included, the imbalances between long-term costs and the amount of budget authority set aside become even greater. Under five sets of assumptions concerning future housing expenses and tenant incomes, the projected long-term costs and budget authority shortfalls for the three programs are as follows:

- The 15-year costs of Section 8 existing housing subsidy commitments entered into in fiscal year 1980 range from $45,600 to $59,000 per housing unit. Long-term costs range from $600 less than the amount of budget authority reserved to $12,800 more than the amount of funds available for each unit of housing.

TABLE S-1. BUDGET AUTHORITY RESERVED FOR FISCAL YEAR 1980 SECTION 8 AND PUBLIC HOUSING SUBSIDY COMMITMENTS AND PROJECTED LONG-TERM COSTS PER UNIT UNDER VARYING ASSUMPTIONS REGARDING FUTURE INCREASES IN HOUSING EXPENSES AND TENANT INCOMES: IN DOLLARS a/

Program	Duration of Commitment (in years)	Budget Authority Reserved b/	Direct Subsidy Cost c/	Total Direct and Indirect Cost d/
Section 8 Existing Housing	15	46,200	45,600 - 59,000	45,600 - 59,000
Section 8 New Construction/ Substantial Rehabilitation	20	101,900	94,700 - 151,800	97,800 - 154,800
	30	152,900	161,200 - 343,400	173,100 - 361,500
	40	203,900	242,600 - 710,300	272,800 - 756-800
Public Housing	40	141,600	226,800 - 426,800	268,400 - 491,000

SOURCE: CBO estimates.

a/ Projected costs are based on current program conditions. Assumptions regarding future increases in housing expenses and tenant incomes range from a low-cost case in which expenses and incomes increase at the rate by which they grew over the 1957-1977 period to a high-cost case in which future increases are based on CBO economic projections for fiscal year 1981. See text and the Appendix for a complete description of the assumptions used.

b/ The amount of budget authority reserved to cover new assistance commitments is calculated using procedures currently employed by HUD.

c/ Direct subsidy costs for the Section 8 program include rental assistance payments and administrative fees, as appropriate. Direct subsidy costs for public housing include debt-service payments and annual operating subsidies.

d/ Indirect costs include mortgage-interest subsidies under the Section 8 new construction/substantial rehabilitation program and foregone revenues on tax-exempt bonds for both Section 8 new construction/substantial rehabilitation and public housing projects. Tax treatments unique to subsidized rental housing projects are included in the indirect costs of Section 8.

- The direct subsidy costs of Section 8 new construction/substantial rehabilitation commitments made in fiscal year 1980 are projected to be as much as three times as great as the amount of budget authority being set aside. Direct 20-year costs are from $94,700 to $151,800 per unit, ranging from $7,200 less to nearly $50,000 more than the available budget authority. Direct subsidy costs for 30-year commitments vary from $161,200 to $343,400; 40-year costs go from $242,600 to 710,300, or up to $500,000 more than the amount of budget authority available. Indirect financing subsidies and tax expenditures add up to $46,500 to long-term costs.

- The long-term direct costs of public housing exceed the amount of budget authority reserved, because funds are not provided at the outset to cover annual operating subsidies. Total 40-year direct expenditures for fiscal year 1980 public housing subsidy commitments range from $226,800 to $426,800. The total of all direct and indirect 40-year costs ranges from $268,400 to $491,000 per unit.

Comparative Program Costs

Because of variations in the duration of commitments made under different housing assistance programs, comparisons of total program costs do not provide a *fair* picture of relative expenses. A comparison of average annual expenditures in constant fiscal year 1980 dollars over the lives of the subsidy commitments presents a better characterization of relative program costs. Average annual constant dollar cost figures are also more directly comparable to the yearly appropriations requests that appear in the federal budget for programs that are not funded in advance.

Among current housing assistance programs, Section 8 existing housing is the least costly, with public housing somewhat less expensive than the Section 8 new construction/substantial rehabilitation program (see Table S-2). The average annual constant dollar cost of serving the same mix of households in each of the three programs ranges from $1,560 to $1,750 per unit in Section 8 existing housing, from $2,200 to $2,530 in public housing, and from $2,490 to $3,510 per unit for the Section 8 new construction/substantial rehabilitation program. The

differences in costs between the Section 8 existing housing program and the new construction programs are due primarily to the lower rent levels in existing housing. The cost differentials between public housing and the Section 8 new construction/substantial rehabilitation program reflect differences in the subsidy mechanisms and may also reflect differences in the quality of the housing provided. Differences in the rules for calculating tenant rent payments increase the cost of public housing relative to the cost of both Section 8 existing housing and the Section 8 new construction/substantial rehabilitation program.

TABLE S-2. PROJECTED AVERAGE ANNUAL COST PER UNIT FOR FISCAL YEAR 1980 SECTION 8 AND PUBLIC HOUSING SUBSIDY COMMITMENTS ASSUMING IDENTICAL TENANT INCOMES: IN FISCAL YEAR 1980 DOLLARS

Program	Length of Commitment (In Years)	Range of Constant Dollar Costs a/
Section 8 Existing Housing	15	1,560 - 1,750
Section 8 New Construction/Substantial Rehabilitation	20	2,750 - 3,300
	30	2,590 - 3,390
	40	2,490 - 3,510
Public Housing	40	2,200 - 2,530

SOURCE: CBO estimates.

a/ Costs are calculated under five sets of assumptions regarding future increases in housing expenses and tenant incomes. See text and the Appendix for a description of the specific assumptions used.

ALTERNATIVE BUDGETARY TREATMENTS

As an alternative to the current procedure for estimating long-term budget authority requirements of the Section 8 program, the Congress could direct that, in the future, calculations of long-term spending needs be based on an analysis of all of the factors that can affect costs. In its funding requests, HUD could be required to consider not only the duration of subsidy commitments and expected starting rent levels (as they do now), but also the anticipated incomes of the tenants, the shares of their incomes that they are expected to contribute toward their own housing expenses, and the rates by which rents and incomes are assumed to change over time. Under such a system, the Congress could be certain that, if specific conditions held, the amount of budget authority set aside for each Section 8 unit would be sufficient to cover long-term costs. Because only the debt-service costs are advance funded in the public housing program, there is less uncertainty involved in estimating multi-year budget authority requirements.

In order to provide more comprehensive estimates of program costs than are now contained in the budget, the Congress could require that future budget documents include estimates of the total of all direct and indirect costs of proposed subsidy commitments for all housing assistance programs. Such estimates, expressed as average annual constant dollar values, would be more directly comparable across programs.

OPTIONS FOR REDUCING COSTS

There are several options available to the Congress for reducing the costs of housing assistance programs. Each contains potential risks as well as potential savings.

Rely More on Existing Housing Assistance. Substantial savings could be realized by providing a greater proportion of rental assistance through programs that subsidize families living in existing housing units. A shift toward greater reliance on existing housing programs might, however, reduce the net effect of federal housing assistance programs in expanding the supply of housing.

Increase the Percent of Income that Tenants are Charged in Rent. Raising tenant rent payments from the present level of

between 15 and 25 percent of income would lower federal expenditures while still providing a substantial subsidy to those households receiving assistance. Smaller, but still appreciable, savings could be achieved by raising tenant rent payments in public housing to the levels currently charged in the Section 8 program. Such changes could be phased in over a number of years to reduce hardships for the lowest-income tenants.

Serve Tenants with Higher Incomes. Some savings could be realized by serving persons with higher incomes, because tenants are charged a fixed percentage of their income in rent, and rent receipts offset federal expenditures. Although such a change would reduce housing subsidy costs, it would also direct aid to persons less in need of assistance.

Eliminate the Rent Ceiling in the Section 8 Existing Housing Program. Because Section 8 existing housing tenants are forbidden from renting units costing more than HUD-established maximums, there is continuing pressure to raise the maximum rent schedules--and, thus, federal outlays--in order to expand housing opportunities. It might be possible to reduce this pressure, and thus reduce the long-term costs of the Section 8 existing housing program, by eliminating the rent ceilings and replacing them with benchmark rental levels that would be used to set assistance payments but would not constrain recipients' housing choices. Assistance payments could be fixed at the difference between the benchmark amount and the required tenant contribution.

Other ways of reducing costs include: making assistance payments directly to tenants in the Section 8 existing housing program; limiting development costs in the Section 8 new construction/substantial rehabilitation program; altering the procedure for fixing yearly rent increases in Section 8 new construction/substantial rehabilitation projects; relying more heavily on the purchase of existing, standard units for use as public housing; and altering the procedure for determining annual adjustments in allowable operating expenses in public housing.

CHAPTER I. INTRODUCTION

The federal government provides housing assistance to a large and growing number of lower-income persons through several different rental assistance programs. Approximately 2.3 million low- and moderate-income households are currently receiving rental assistance under programs administered by the Department of Housing and Urban Development, and through fiscal year 1979 funds have been provided to aid a total of 3.5 million households. The President's budget submission for fiscal year 1980 requests funds to extend assistance to an additional 300,000 lower-income renters. In 1980, outlays for rental assistance are expected to total $5 billion. At the rate at which new commitments are now being made, federal expenditures for rental assistance could total $9 billion by fiscal year 1984.

All rental assistance programs involve multiyear obligations on the part of the federal government. Assistance commitments made in one year, therefore, will require direct outlays and, in many cases, foregone tax revenues for up to 40 years in the future. For each program, funding is provided to cover at least a portion of the long-term direct expenditures at the time that a new commitment is made. However, the amount of long-term spending authority--budget authority--provided in advance may not be sufficient to cover that portion of the total program costs that it is expected to cover. Also, some direct expenditures associated with housing assistance programs are not funded in advance, nor are indirect subsidy costs and tax expenditures explicitly considered when new commitments are made.

The budgetary treatment of housing assistance programs, thus, presents the Congress with two important issues as it faces the annual decision concerning the number of additional households to be aided and the level of funding to be authorized to pay for the additional assistance:

- Will the amount of budget authority set aside to fund new subsidy commitments be adequate to cover actual multiyear expenditures, or will additional spending authority be needed in the future?

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- What will the total cost be, including both direct expenditures and foregone tax revenues, for subsidy commitments made under different programs and how can the long-term costs of housing assistance programs be reduced?

This paper addresses these issues. It presents estimates of the long-term costs of rental assistance programs, taking into account factors not explicitly considered under current funding procedures; compares projected direct subsidy costs of fiscal year 1980 commitments to the amount of budget authority likely to be reserved to fund those commitments; and provides estimates of total program costs that permit comparisons among housing assistance programs and are more nearly comparable to the costs of nonhousing programs that are not funded in advance. 1/ Chapter II presents estimates of the costs of the Section 8 housing assistance payments program. In Chapter III, the long-term costs of the public housing program are examined. Chapter IV compares program costs and discusses the reasons for the differences that exist. Alternatives to the current budgetary treatment of housing assistance programs are discussed in Chapter V, and options for reducing program costs are presented in Chapter VI.

1/ The cost estimates presented in this paper require numerous assumptions concerning current and future program conditions. Wherever possible, actual program data have been used as the basis for assumptions concerning present conditions, however, such data have not always been available. Assumptions regarding long-term economic and programmatic circumstances are based on past trends as well as current conditions and are meant to cover a range of plausible futures. In every instance, the assumptions made in preparing the cost estimates are stated explicitly. Alternative assumptions could result in quite different cost projections. None of the estimates presented here should be viewed as predictions of the future. Rather, the figures presented in this paper describe what program costs will be if specific conditions hold.

CHAPTER II. LONG-TERM COSTS OF THE SECTION 8 HOUSING ASSISTANCE PAYMENTS PROGRAM

The Section 8 housing assistance payments program, which was authorized in 1974, 1/ is becoming the federal government's principal mechanism for providing housing subsidies. Through the end of fiscal year 1978, there were outstanding commitments to assist about 1.2 million households in Section 8 housing. Approximately 300,000 additional Setion 8 subsidy commitments are expected to be made during fiscal year 1979 and the Administration's 1980 budget submission requests funding for 250,000 further commitments.

Under the Section 8 program, the government pays a share of the housing costs of lower-income families and individuals living in existing, newly built, or substantially rehabilitated rental housing. Because the assistance payments are made through multiyear contracts entered into by the federal government, an amount of long-term budget authority assumed to be sufficient to pay the annual subsidy for the length of the commitment must be set aside when a new Section 8 assistance commitment is made. In recent years, the adequacy of the method used to estimate long-term spending requirements for Section 8 and the amount of budget authority being reserved to cover long-term costs have been questioned. There has also been concern over the total cost of the Section 8 program, including indirect financing subsidies and tax expenditures that are not a part of the direct assistance payments.

This chapter describes the Section 8 funding procedures, presents projections of the long-term direct subsidy costs of Section 8 commitments made in fiscal year 1980, and compares these costs to the amount of budget authority likely to be

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1/ Section 8 of the United States Housing Act of 1937, as amended by the 1974 Housing and Community Develpment Act (P.L. 93-383).

reserved to fund the commitments. 2/ Estimates of total program costs, including direct rental assistance payments, indirect financing expenses and tax expenditures, are also presented.

THE NATURE OF THE SUBSIDY COMMITMENT AND CURRENT FUNDING PROCEDURES

Under the Section 8 program, the federal government pays the owners of rental housing the difference between the rent due on their units--not to exceed government-established maximums--and the amount that tenants pay toward their own housing expenses, which is set by law at between 15 and 25 percent of family income. For existing privately owned units, the subsidy commitment takes the form of a contract between the Department of Housing and Urban Development (HUD) and a state or local housing agency, which enrolls persons in the program, certifies that the units they choose meet minimum physical standards, and makes payments to their landlords. The contract, which specifies the number of households to be assisted, runs for five years and is renewable at the option of the local agency for up to a total of 15 years. For newly built and substantially rehabilitated housing, HUD contracts with a private project sponsor (or, in rare cases, a public agency) who develops and retains ownership of the units. Section 8 new construction/substantial rehabilitation commitments may run for as long as 40 years.

In any given year of a multiyear assistance commitment, the federal expenditure will depend on the rents of the units occupied and the amount that tenants contribute toward their own housing expenses. As rents and tenant contributions increase, the size of the subsidy will change. 3/ The long-term cost

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2/ Cost estimates are presented for the Section 8 existing housing program and the Section 8 new construction/substantial rehabilitation program. Because of the lack of data, estimates are not presented for the moderate rehabilitation program that is being implemented for the first time in fiscal year 1979.

3/ The annual subsidy will increase even if rents and tenant contributions grow at the same rate. Because the rent level is higher than the tenant payment at the outset, the same percent change applied to the two will widen the gap between them.

to the government of each commitment, therefore, depends on several factors: (1) the duration of the assistance contract; (2) starting rent levels; (3) initial tenant incomes and the share of income they contribute toward rent; and (4) the rates by which rents and tenant incomes increase.

The procedure currently used by HUD to determine the amount of budget authority to be reserved for each new subsidy commitment explicitly considers only two of the factors that affect long-term costs. For each new commitment, the amount of budget authority to be set aside is calculated by multiplying the maximum starting rent by the maximum number of years that the commitment might run. (For example, if the annual rent in the first year were $3,000 and the maximum contract term were 30 years, the amount of budget authority reserved would be $90,000.) 4/ The total amount of budget authority reserved for each commitment represents the maximum contractual obligation of the federal government. The actual federal payment in any year, however, will be equal to the gap between the then-current rent level and the tenant contribution. In the early years of a subsidy commitment, outlays will be less than the annual share of the budget authority available, but increases in rents and tenant incomes will likely widen the rental gap in later years, thereby increasing federal expenditures. There is an assumption implicit in the procedure now used to calculate budget authority set-asides that tenant contributions in the early years of a subsidy commitment and subsequent increases in tenant contributions will be sufficient to cover needed rent increases over the life of the assistance agreement. If actual subsidy needs exceed the amount of budget authority reserved at the outset, the annual assistance payments will have to be diminished, the duration of the commitment shortened, or additional spending authority provided.

4/ The annual share of long-term spending authority (in this case, $3,000) is referred to as contract authority. Each year's appropriation for assisted housing programs provides HUD with additional long-term budget authority and an associated amount of contract authority. Under present funding procedures, both of these values limit the number of subsidy commitments that can be entered into. Starting rent levels determine how many additional units the contract authority will support, and the duration of the commitments determine how far the budget authority can be stretched.

DETERMINANTS OF DIRECT SUBSIDY COSTS

The estimates of long-term costs presented in this chapter employ a methodology that explicitly takes into account all of the factors that can affect eventual subsidy expenses.

The Duration of Subsidy Commitments

The duration of Section 8 assistance commitments varies with the kind of unit subsidized. All subsidy commitments for existing housing carry maximum terms of 15 years. New construction and substantial rehabilitation assistance contracts may run for as long as 40 years, depending on the type of project sponsor and the nature of the financing (see Table 1). About 60 percent of the fiscal year 1978 new construction and substantial rehabilitation subsidy commitments were for 20 years, with the remainder divided among 30- to 40-year commitments. Operating plans for fiscal year 1979 call for shifting certain of the lengthier new construction/substantial rehabilitation commitments to shorter terms. 5/

Initial Rent Levels

Initial rents in Section 8 units affect first-year program costs and serve as the base upon which future rent increases are built. Starting rents in the Section 8 existing housing program are governed by HUD-established maximum allowable rents for each

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5/ Given current procedures for determining the amount of budget authority to be reserved for each subsidy commitment, a shift toward shorter-term contracts will permit more commitments to be made with available budget authority. However, if the federal government has guaranteed the financing for a period extending beyond the end of the subsidy commitment--as is frequently the case--it may prove necessary to provide additional Section 8 assistance when the initial contracts run out in order to maintain the financial viability of the projects and avoid default.

TABLE 1. MAXIMUM DURATION OF SECTION 8 SUBSIDY COMMITMENTS AND TENTATIVE OPERATING PLAN FOR FISCAL YEAR **1979** BY TYPE OF PROJECT AND DEVELOPMENT METHOD, AND TYPE OF FINANCING USED

Type of Project and Development Method	Type of Financing	Maximum Duration of Commitment (in years)	Number of Commitments Planned (in units) a/
Existing Housing		15	123,100 b/
New Construction and Substantial Rehabilitation			
Section 202 Housing for the Elderly and Handicapped	Direct Federal Loans	20	27,700
Farmers Home Administration Mortgage-Subsidy Projects	Direct Federal Loans	20	10,000
Private Developer-Sponsored and Joint Public Housing Agency/Private Developer-Sponsored Projects	Federally Insured Mortgages	20	71,900
	Uninsured Mortgages	30	36,100
State Housing Finance Agency-Financed Projects	Tax-Exempt Bonds	30	22,300
		40	13,200

SOURCE: HUD Office of Budget.

a/ Includes commitments to be financed with funds carried over from fiscal year 1978.

b/ Includes approximately 39,000 commitments under the moderate rehabilitation program being implemented for the first time in fiscal year 1979.

market area--referred to as fair market rents (FMRs). 6/ Except by waiver from HUD or the local agency administering the program, Section 8 tenants cannot occupy units renting for more than the applicable FMR. Tenants may, of course, select units renting below the fair market rent level. 7/ The schedule of FMRs for each market area is adjusted annually, permitting rents to increase each year.

For new construction and substantial rehabilitation projects, the assistance agreement between HUD and the project sponsor specifies the rents to be charged after construction is completed and the units are available for occupancy. These rents are based on market-wide fair market rent schedules and assessments by HUD as to the reasonableness of the rents for each particular project. The agreed upon rents are meant to incorporate inflation in development and operating costs over a two-year period between the initial subsidy commitment and the completion of construction. HUD may, however, grant rent increases at the time that construction is completed to compensate the owner for unavoidable construction delays and for other cost increases that are not the fault of the project sponsor and that could not have been foreseen at the time that the subsidy agreement was entered into. In the years following initial occupancy, automatic annual rent adjustments are made to cover increases in operating expenses and to keep rents at a level

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6/ All FMRs for existing housing are expressed as "gross rent" ceilings and include both the contract rent payment due the landlord and the cost of utilities that may or may not be included in the contract rent. Separate utility allowance schedules specify the amount by which the maximum allowable rent level is to be reduced for each utility that the tenant must pay for directly. The tenant's monthly payment to his landlord is also reduced by the amount of any applicable utility allowance. If the utility allowances accurately reflect actual costs, the total housing expense for the tenant will remain the same regardless of whether or not utilities are included in the contract rent.

7/ As of October 1976, actual gross rents in Section 8 existing housing averaged 6 percent below the applicable fair market rent. This ratio was applied in preparing all of the cost estimates appearing in this paper.

roughly equivalent to that in comparable unsubsidized projects. Owners may also petition HUD for exceptional rent increases if unique circumstances warrant them.

Actual starting Section 8 rents vary widely by subprogram, local market, and unit size (see Table 2). For existing housing subsidy commitments entered into in fiscal year 1978, the average annual gross rent ceiling was $2,641 per year. For new construction and substantial rehabilitation commitments made in the same year (units expected to become available for occupancy for the first time in fiscal year 1980), the average annual gross rent, including utility costs paid directly by the tenant, is estimated to be $4,499.

Initial Tenant Incomes and Contributions Toward Rent

Long-term Section 8 costs will depend, in part, on the incomes of persons receiving assistance and the shares of their incomes that they pay toward rent. By law, Section 8 assistance is limited to lower-income families and individuals, with preference among single-person households given to elderly, handicapped, or displaced persons. At least 30 percent of the tenants in any project must be very low-income households. 8/ Most

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8/ Maximum allowable family incomes for eligibility as lower-income or very low-income are indicated in the following table. All income-eligibility determinations are based on gross incomes and do not take into account deductions that apply in determining the income used to calculate tenant rent contributions.

Family Size	Family Income as Percent of Median Income for all Families in the Area	
	Lower-Income	Very Low-Income
1 person	50	30
2	64	40
3	72	45
4	80	50
5	85	54
6	90	58
7	95	62
8 or more	100	66

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TABLE 2. ESTIMATED ANNUAL STARTING GROSS RENTS FOR FISCAL YEAR 1978 SECTION 8 ASSISTANCE COMMITMENTS: IN DOLLARS

Program	Number of Bedrooms a/					Average, All Units
	Zero	One	Two	Three	Four or More	
Existing Housing b/	1,993	2,259	2,657	2,989	3,321	2,641
New Construction and Substantial Rehabilitation c/	3,832	4,057	4,508	5,072	5,635	4,299

SOURCE: Derived from HUD management information system reports.

a] Rent levels by number of bedrooms are estimates based on ratios in published fair market rent schedules.

b/ Average rents for the existing housing program are for commitments that add to the total inventory of subsidized units. Figures do not include either amendments to earlier assistance contracts or commitments that provide additional subsidies for assisted housing developed under other programs without adding to the total number of households receiving aid.

c/ Average rents for the new construction/substantial rehabilitation program exclude projects developed under other programs and converted to Section 8 housing. Also excluded are assistance commitments made in conjunction with Farmers Home Administration (FmHA) rental projects, most of which carry subsidized mortgages. (Rents in non-FmHA projects located outside of metropolitan areas were substituted for FmHA project rents in calculating the national average.)

families receiving Section 8 assistance are required to contribute 25 percent of their adjusted income toward their housing expenses. 9/ The maximum tenant contribution rate is 15 percent of total unadjusted income for very-low income families with 6 or more minors, low-income families with eight or more minors, families with exceptional medical or other unusual expenses in excess of one-fourth of their income, and all tenants for whom 25 percent of adjusted income is less than 15 percent of unadjusted income.

The average income of Section 8 tenants is well below the maximum allowable level. Of families entering the Section 8 existing housing program from July through December 1977, the average annual income, before deductions, was $3,938 (see Table 3). The average annual income for first-time residents of new construction and substantial rehabilitation projects was $4,476. Average incomes vary widely among different types of households. In the existing housing program, average annual incomes as of 1977 ranged from $2,988 for single-person nonelderly households to $5,614 for nonelderly households with five or more members. Average incomes among families moving into new construction/substantial rehabilitation projects ranged from $3,407 for single-person elderly households to $6,588 for nonelderly-headed households with five or more members.

The average percent of income paid in rent differs somewhat between the two Section 8 programs and varies widely among different types of households. The average percent of income paid toward housing by new tenants was 22 percent in existing housing and 23.5 percent in new construction/substantial rehabilitation projects as of 1977. Among different types of households, average contribution rates ranged from about 19 percent to 25 percent of unadjusted income.

Because tenant incomes and contribution rates--as well as average rents--differ by type of household, long-term Section 8 costs will be affected by the mix of households served. At the present time, the Section 8 existing housing program is heavily

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9/ In determining annual adjusted income, a deduction of $300 is allowed for each minor. Deductions are also allowed for medical expenses in excess of 25 percent of income and for certain unusual expenses.

TABLE 3. AVERAGE INCOME AND AVERAGE PERCENT OF INCOME PAID IN RENT FOR FIRST-TIME SECTION 8 TENANTS, JULY 1977 THROUGH DECEMBER 1977: BY HOUSEHOLD TYPE

Program	Nonelderly-Headed Households				
	One Person	Two Persons	Three Persons	Four Persons	Five or More Persons
Existing Housing					
Average income (in dollars)	2,988	3,642	4,237	4,776	5,614
Average percent of income paid in rent a/	24.5	22.8	20.9	19.8	18.5
Proportion of new tenants (in percents)	1.3	17.5	16.2	9.9	9.4
Estimated proportion of FY 1978 subsidy commitments (in percents) b/	1.8	24.6	22.6	13.8	13.2
New Construction/Substantial Rehabilitation					
Average income (in dollars)	5,463	5,009	5,712	6,101	6,588
Average percent of income paid in rent a/	25.0	25.0	22.2	21.1	19.7
Proportion of new tenants (in percents)	3.7	14.0	10.7	7.0	4.4
Estimated proportion of FY 1978 subsidy commitments (in percents) b/	3.9	14.8	11.3	7.4	4.6

SOURCE: HUD management information system report, December 31, 1977.

a/ Average percent of income paid in rent for each type of household is an estimate derived from HUD *data;* the average for all households is taken directly from the HUD report. All figures are expressed as a percent of unadjusted income.

(Continued)

TABLE 3. (Continued)

Program	Elderly-Headed Households: One Person	Two Persons	Three or Four Persons	Five or More Persons	All Households
Existing Housing					
Average income (in dollars)	3,074	4,259	4,543	5,408	3,938
Average percent of income paid in rent a/	25.0	21.7	22.3	20.7	22.0
Proportion of new tenants (in percents)	33.2	8.3	2.9	1.2	100.0
Estimated proportion of FY 1978 subsidy commitments (in percents) b/	17.5	4.4	1.5	0.6	100.0
New Construction/Substantial Rehabilitation					
Average income (in dollars)	3,407	5,348	5,287	5,404	4,476
Average percent of income paid in rent a/	25.0	21.1	24.2	23.0	23.5
Proportion of new tenants (in percents)	50.2	8.4	1.2	0.4	100.0
Estimated proportion of FY 1978 subsidy commitments (in percents) b/	48.4	8.1	1.1	0.4	100.0

b/ The estimated distribution among households for fiscal year 1978 commitments is based on the split between elderly and nonelderly units and the expected distribution of households by size within each age group.

weighted toward nonelderly-headed households. The new construction/substantial rehabilitation program, on the other hand, is serving primarily elderly households and small families but is beginning to shift somewhat toward more projects for larger families. Cost estimates reported here assume that for both the existing housing and new construction/substantial rehabilitation programs, the fiscal year 1978 mix of commitments between elderly and nonelderly households will hold in fiscal year 1980 as well. 10/

Increases in Rents and Tenant Incomes

The long-term costs of Section 8 depend greatly on the rates of increase in rents and tenant incomes. The larger the increase in rents, the greater the long-term costs; the larger the increase in tenant incomes, the greater the amount tenants pay toward their own housing expenses, and, therefore, the lower the long-term costs. Although it is not possible to predict the rate by which either rents or incomes will increase over periods as long as 40 years, it is possible to calculate long-term program costs under different assumed increases in rents and incomes.

Five different sets of assumptions concerning future increases in rents and tenant incomes were employed in preparing the cost projections presented in this paper. For existing housing commitments made in fiscal year 1980, the first full year of subsidy payments is assumed to be fiscal year 1981. Rents in the existing housing program are assumed to rise at the rate by which gross rents are projected to increase market-wide, reflecting both increases in the rents of already existing units and the effect of more expensive, newly built units on average market rents. In the case of the new construction/substantial rehabilitation program, subsidy commitments entered into in fiscal year 1980 are not assumed to result in fully occupied projects until fiscal year 1983 because of the time needed to build and rent the housing. During the construction period, rents remain fixed at the levels set in the assistance agreement between HUD and the project sponsor, but the income of potential tenants can be expected to continue to increase. Following initial occupancy,

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10/ A substantial shift in the tenant mix could alter long-term program costs.

the rents in newly built or substantially rehabilitated projects are assumed to increase at the rate by which rent in already occupied units are projected to grow--a slower rate of increase than is assumed to apply to the Section 8 existing housing program.

The assumptions used cover a range of underlying inflation rates from less than 4 percent (Case 1) to greater than 7 percent (Case 5). The first three cases are based on increases in housing expenses and household incomes for different periods in the past. Cases 4 and 5 are based on two projections of future economic circumstances--one relatively optimistic and the other quite pessimistic. The specific assumptions, described in greater detail in the Appendix, are as follows:

Case 1. The rate of increase in rents phases down between now and fiscal year 1984 to an annual rate equivalent to the amount by which gross rents grew from 1957 to 1977--an estimated yearly increase of 3.8 percent market-wide and 3.1 percent in already occupied units--well below the current rate of increase. Increases in tenant wage income level off by fiscal year 1984 at the rate by which the average hourly wage grew between 1957 and 1977, or 5.3 percent per year; retirement benefits and public assistance payments to tenants increase at the annual rate by which the Consumer Price Index (CPI) grew over that period, or 3.9 percent. 11/

Case 2. After a five-year phase-in, the economic circumstances of the 1962-1977 period prevail. Beginning in fiscal year 1984, market-wide rents increase at an annual rate of 4.3 percent and rents in already occupied units grow at 3.6 percent per year. Starting in fiscal year 1984, tenant wage income increases at 5.9 percent annually; benefit

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11/ In the past, increases in public assistance payments have not always kept pace with inflation. The assumption that welfare payments will grow at the rate of increase in the CPI may, therefore, overstate future tenant incomes. If public assistance payments increase more slowly than the CPI, average tenant incomes will grow more slowly and long-term program costs will be greater.

and welfare payments grow by 4.7 percent a year, the rate by which the CPI increased from 1962 to 1977.

Case 3. Rent increases slow down over the next five years to an annual rate equivalent to the amount by which gross rents rose between 1967 and 1977, an annual increase of 5.6 percent market-wide and 4.9 percent for already occupied units. The rate of increase in tenant income from wages levels off by fiscal year 1984 at 7.1 percent per year. Increases in benefit and welfare payments level off at 6.1 percent annually--the average increase in the CPI between 1967 and 1977.

Case 4. The rate of inflation in rents phases down over the next five years to an annual increase of 6.9 percent market-wide and 6.3 percent for already occupied housing, consistent with CBO economic projections for the period through fiscal year 1984. The rate of increase in tenant income from wages levels off after five years at 7.5 percent per year--the projected rate of increase in the average hourly wage for fiscal year 1984. Benefit and welfare payments increase by 6.1 percent per year--the projected rate of increase in the CPI.

Case 5. Beginning in fiscal year 1981, rents increase by 7.7 percent per year market-wide and by 7.0 percent annually for already occupied units, consistent with the CBO economic projections for that year. Beginning in fiscal year 1981, tenant wage income increases at the projected annual rate of growth in the average hourly wage for that year, 8.0 percent. Benefit and welfare payments to tenants increase by 7.3 percent per year--the projected rate of growth in the CPI for fiscal year 1981.

INDIRECT EXPENDITURES

The Section 8 new construction/substantial rehabilitation program involves indirect costs to the federal government in

addition to the rental assistance payments that are required under the subsidy contracts. Indirect expenditures include mortgage-interest subsidies for privately financed projects and foregone revenues from tax-exempt bonds used to pay the development costs of publicly financed projects. Owners of Section 8 projects also enjoy favorable tax treatments not available to persons owning unsubsidized housing.

Mortgage-Interest Subsidies for Privately Financed Projects

Many privately sponsored Section 8 new construction/substantial rehabilitation projects are financed through reduced-interest federally insured mortgages that are written by private lenders and sold to the Government National Mortgage Association (GNMA)--an agency of HUD--which then resells the loans as market-rate-yield investments. Under this arrangement, GNMA absorbs the difference in interest rates as a financing subsidy, with the full cost borne by GNMA at the time that the mortgage is sold. Because this tandem financing assistance is funded through the GNMA Special Assistance Functions Fund, which also supports other types of mortgage assistance, the mortgage-subsidy costs directly attributable to the Section 8 program are not clearly identified in all budget documents.

The cost estimates presented here assume that one-half of the 20-year Section 8 new construction and substantial rehabilitation assistance commitments made in fiscal year 1980 will employ tandem financing. The interest rate on the tandem-assisted mortgages is assumed to be 7.5 percent and the cost to GNMA of increasing the yield to that of a market rate investment is assumed to be 14 percent of the value of the mortgage. 12/

Tax Expenditures

Many Section 8 new construction and substantial rehabilitation projects--including all those sponsored by state housing finance agencies--are financed by state or local housing development bonds. Because the interest paid to the purchasers of such bonds is exempt from federal taxation, the interest rate may be

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12/ This is consistent with GNMA's recent experience.

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set at a lower level than the prevailing rate for taxable investments. This reduces the financing costs that must be carried in the project rents. However, the tax exemption also results in a revenue loss that represents a significant component of the total cost of the Section 8 program to the federal government. The cost projections presented here assume that purchasers of tax-exempt bonds would otherwise have bought taxable investments with average yields of two percentage points greater than the prevailing rate of inflation. The average marginal tax rate of persons purchasing the bonds is assumed to be 35 percent.

Owners of newly built or substantially rehabilitated Section 8 housing projects receive certain favorable tax treatments that are not accorded to owners of unsubsidized rental housing. Owners of all newly built rental housing (both subsidized and unsubsidized) are permitted to depreciate the value of the units for tax purposes at a 200 percent declining balance rate, resulting in greater tax losses in the early years of a project's life than would occur for nonhousing investments. Owners of newly built subsidized projects, however, are subject to less stringent rules regarding the eventual taxation of the excess depreciation when the property is sold, providing an additional tax benefit. Owners of substantially rehabilitated subsidized projects are allowed to write off the entire rehabilitation expenses over five years, considerably faster than would be permitted even under the 200 percent declining balance depreciation method. Builders of all subsidized housing projects also still enjoy the full benefits of provisions that permit interest and property tax payments made during construction to be treated as current business expenses for federal tax purposes, rather than being included in the cost of construction and written off over the life of the building. This substantial federal tax benefit, which, until recently, has been available to the builders of all new rental housing, is currently being phased down for unsubsidized housing and will begin to be phased down for subsidized projects in 1982. 13/

The cost estimates appearing here consider the tax provisions that will be in effect when construction is begun on Section 8 projects approved in fiscal year 1980. Only the

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13/ For a more complete discussion of real estate tax shelters, see Congressional Budget Office, Real Estate Tax Shelter Subsidies and Direct Subsidy Alternatives (May 1977).

difference in tax expenditures between subsidized and unsubsidized housing is counted as an expense attributable to the Section 8 program. 14/ The total federal tax expenditure associated with Section 8 projects--including the benefits available to all rental housing investments as well as the benefits available only to subsidized housing--is several times larger.

PROJECTED COSTS

The Existing Housing Program

The estimated long-term costs of Section 8 existing housing subsidy commitments made in fiscal year 1980 differ widely, depending on the assumed rates of increase in rents and tenant incomes (see Table 4). Under the five sets of assumptions examined, total long-term costs range from $45,600 to $59,000 per housing unit. For the five scenarios, projected costs are from $600 less than the amount of budget authority available to $12,800, or 28 percent, more than the amount of funds reserved. 15/ Even for the most pessimistic case, the amount of budget authority provided will be adequate to pay the subsidy costs for 12 of the 15 years. Under current funding procedures, the amount of budget authority reserved when a subsidy commitment is made does not depend on assumed future economic and programmatic conditions.

Because the long-term costs of the Section 8 existing housing program include the effect of 15 years of price increases, expense figures for this program are not directly

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14/ The cost estimates do not include the tax expenditure resulting from the five-year write-off of substantial rehabilitation expenses, over and above the effect of the 200 percent declining balance depreciation.

15/ The budget authority set-asides appearing in this paper do not agree with the estimated per-unit cost figures presented in the 1980 HUD budget request, because the Administration has assumed a lower rate of inflation between fiscal years 1978 (when the latest actual program cost data are available) and 1980. Also, HUD has assumed that the rate of increase in per-unit costs will be slowed by a number of program changes now under consideration.

TABLE 4. BUDGET AUTHORITY AVAILABLE AND PROJECTED LONG-TERM COST PER UNIT FOR SECTION 8 EXISTING HOUSING SUBSIDY COMMITMENTS ENTERED INTO IN FISCAL YEAR 1980 UNDER VARIOUS ASSUMPTIONS REGARDING FUTURE INCREASES IN RENTS AND TENANT INCOMES: IN DOLLARS

Assumption a/	Available Budget Authority b/	Projected Long-Term Cost c/	Difference Between Available Budget Authority and Projected Long-Term Cost d/
Case 1 (3.9 percent inflation)	46,200	45,600	+ 600
Case 2 (4.7 percent inflation)	46,200	46,400	- 200
Case 3 (6.1 percent inflation)	46,200	49,300	- 3,100
Case 4 (6.1 percent inflation)	46,200	55,500	- 9,300
Case 5 (7.3 percent inflation)	46,200	59,000	- 12,800

SOURCE: CBO estimates.

a/ See text and Appendix for a description of the assumptions used.

b/ Available budget authority is calculated using procedures currently applied by HUD.

c/ The cost projections include a $275 per-unit initial administrative fee paid by HUD to the local agency and an ongoing fee for each unit under lease equal to 8.5 percent per month of the fair market rent of a two-bedroom unit.

d/ + = Excess budget authority
- = Insufficient budget authority

comparable with the annual expenditures that appear in federal budget documents for programs that are not advance funded. One means of expressing housing assistance program costs in terms that are more directly comparable to those for annually funded programs is to translate the multiyear costs into average annual constant dollar expenses. When expressed in terms of the average annual constant dollar expenditures, the difference in costs across different future conditions is greatly diminished (see Table 5). Whereas the average annual federal expenditure for each additional Section 8 existing housing commitment to be made in fiscal year 1980 ranges from $3,040 to $3,930 under the five sets of assumptions considered, the average annual constant dollar cost of those commitments (in terms of fiscal year 1980 dollars) ranges from only $1,980 to $2,170 per unit. In each case, the constant dollar cost is less than the average amount of budget authority available per year--the figure that is now commonly considered to represent the average annual "real" cost of Section 8.

The New Construction/Substantial Rehabilitation Program

The long-term direct subsidy costs of Section 8 new construction/substantial rehabilitation commitments also vary greatly with future program conditions and, in most instances, exceed the amount of budget authority available (see Table 6). Costs are especially variable for the lengthiest subsidy commitments. The long-term direct subsidy costs of 20-year commitments expected to be entered into in fiscal year 1980 range from approximately $94,700 to $151,800 per unit, for the five cases considered. This ranges from $7,200 less than the amount of available budget authority available to nearly $50,000 more than the amount of funds provided. For 30-year commitments, direct subsidy costs vary from about $161,200 to $343,400, or up to $190,000 more than the amount of budget authority available. For 40-year commitments, long-term costs range from $161,200 to $343,400, or up to more than 3 times the amount of budget authority available.

TABLE 5. AVERAGE BUDGET AUTHORITY AVAILABLE PER YEAR AND PROJECTED AVERAGE ANNUAL COST PER UNIT FOR SECTION 8 EXISTING HOUSING SUBSIDY COMMITMENTS ENTERED INTO IN FISCAL YEAR 1980 UNDER VARIOUS ASSUMPTIONS REGARDING FUTURE INCREASES IN RENTS AND TENANT INCOMES: IN CURRENT AND CONSTANT DOLLARS

Assumption a/	Average Amount of Budget Authority Available Per Year	Average Annual Subsidy Cost b/	Average Annual Subsidy in Constant (FY 1980) Dollars b/
Case 1 (3.9 percent inflation)	3,080	3,040	2,050
Case 2 (4.7 percent inflation)	3,080	3,090	2,000
Case 3 (6.1 percent inflation)	3,080	3,310	1,980
Case 4 (6.1 percent inflation)	3,080	3,700	2,170
Case 5 (7.3 percent inflation)	3,080	3,930	2,130

SOURCE: CBO estimates.

a/ See text and Appendix for a description of the assumptions used.

b/ Projected costs include the yearly share of the $275 per unit start-up fee paid to the local administering agency in the first year of each subsidy commitment as well as the ongoing annual administrative fee.

TABLE 6. BUDGET AUTHORITY AVAILABLE AND PROJECTED LONG-TERM DIRECT SUBSIDY COST PER UNIT FOR SECTION 8 NEW CONSTRUCTION/ SUBSTANTIAL REHABILITATION SUBSIDY COMMITMENTS ENTERED INTO IN FISCAL YEAR 1980 UNDER VARIOUS ASSUMPTIONS REGARDING FUTURE INCREASES IN DEVELOPMENT COSTS, RENTS, AND TENANT INCOMES: IN DOLLARS a/

Assumption b/	Length of Commitment (in years)	Available Budget Authority	Projected Long-Term Direct Subsidy Cost	Difference Between Available Budget Authority and Projected Long-Term Direct Subsidy Cost c/
Case 1	20	101,900	94,700	+ 7,200
(3.9 percent	30	152,900	161,200	- 8,300
inflation)	40	203,900	242,600	- 38,700
Case 2	20	101,900	98,300	+ 3,600
(4.7 percent	30	152,900	170,400	- 17,500
inflation)	40	203,900	260,400	- 56,500
Case 3	20	101,900	114,300	- 12,400
(6.1 percent	30	152,900	214,300	- 61,400
inflation)	40	203,900	356,000	-152,100
Case 4	20	101,900	142,000	- 40,100
(6.1 percent	30	152,900	308,600	-155,700
inflation)	40	203,900	610,900	-407,000
Case 5	20	101,900	151,800	- 49,900
(7.3 percent	30	152,900	343,400	-190,500
inflation)	40	203,900	710,300	-506,400

SOURCE: CBO estimates.

a/ Costs include only those incurred through the annual housing assistance contract with the project sponsor. Available budget authority is calculated using procedures currently applied by HUD.

b/ See text and Appendix for description of assumptions used.

c/ + = Excess budget authority; - = Insufficient budget authority.

The average annual cost to the federal government of fiscal year 1980 Section 8 new construction/substantial rehabilitation assistance agreements--including both direct outlays under the assistance contract and indirect financing subsidies and tax expenditures--ranges from $4,890 to $18,920 per unit for the five cases considered (see Table 7). Expressed in constant dollars, total costs range from $2,490 to $3,480 per unit. As with the Section 8 existing housing program, constant dollar costs differ little with the future economic and programmatic circumstances and also vary little with the length of the subsidy commitments.

TABLE 7. AVERAGE BUDGET AUTHORITY AVAILABLE PER YEAR AND PROJECTED AVERAGE ANNUAL COST PER UNIT FOR SECTION 8 NEW CONSTRUCTION/SUBSTANTIAL REHABILITATION SUBSIDY COMMITMENTS ENTERED INTO IN FISCAL YEAR 1980, UNDER VARIOUS ASSUMPTIONS REGARDING FUTURE INCREASES IN DEVELOPMENT COSTS, RENTS, AND TENANT INCOMES: IN CURRENT AND CONSTANT DOLLARS

Assumption a/	Length of Commitment (in years)	Average Amount of Budget Authority Available Per Year	Direct Subsidy Cost Only b/		Total Cost b/	
			Average Annual Cost	Cost in Constant (FY 1980) Dollars	Average Annual Cost	Cost in Constant (FY 1980) Dollars
Case 1	20	5,100	4,740	2,690	4,890	2,820
(3.9 percent	30	5,100	5,370	2,510	5,770	2,710
inflation)	40	5,100	6,070	2,330	6,820	2,660
Case 2	20	5,100	4,920	2,600	5,070	2,720
(4.7 percent	30	5,100	5,680	2,370	6,120	2,580
inflation)	40	5,100	6,510	2,160	7,360	2,490
Case 3	20	5,100	5,710	2,620	5,860	2,740
(6.1 percent	30	5,100	7,140	2,380	7,670	2,590
inflation)	40	5,100	8,900	2,160	9,910	2,490
Case 4	20	5,100	7,100	3,130	7,250	3,250
(6.1 percent	30	5,100	10,288	3,140	10,810	3,350
inflation)	40	5,100	15,270	3,140	16,290	3,480
Case 5	20	5,100	7,590	2,930	7,740	3,050
(7.3 percent	30	5,100	11,450	2,860	12,050	3,070
inflation)	40	5,100	17,760	2,790	18,920	3,110

SOURCE: CBO estimates.

a/ See text and Appendix for a description of the assumptions used.

b/ Direct subsidy costs are those incurred through the annual housing assistance contract with the project sponsor. Total costs include indirect financing subsidies (except interest subsidies paid by the Farmers Home Administration on FmHA-sponsored projects) and tax expenditures. One-half of all 20-year assistance agreements are assumed to carry GNMA tandem mortgage assistance. One-half of the 30-year agreements and all of the 40-year contracts are assumed to be financed through tax-exempt bonds. It is assumed that 75 percent of all project owners (other than the not-for-profit sponsors of Section 202 projects) will avail themselves of the special tax treatments afforded to subsidized housing.

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CHAPTER III. LONG-TERM COSTS OF THE PUBLIC HOUSING PROGRAM

The public housing program was authorized in 1937 and served as the federal government's primary lower-income rental assistance program for nearly 30 years thereafter. As other programs have been implemented, public housing has remained heavily utilized and currently assists more households than any other single program. As of October 1978, approximately 1.1 million households were living in public housing. Another 56,000 subsidy commitments are expected to be made in fiscal year 1979 and funds have been requested to finance 50,000 more commitments in 1980.

Under the public housing program, HUD pays all debt service expenses--including development and financing costs--and a share of the ongoing operating expenses for rental housing that is owned by state and local public housing agencies (PHAs) and leased to lower-income families and individuals at reduced charges. 1/ An amount of budget authority assumed to be sufficient to pay the debt-service cost is reserved at the time that a new subsidy commitment is made. Funds to pay annual operating subsidies, on the other hand, are appropriated in the year in which the money is to be spent. The full direct subsidy costs of public housing commitments are, therefore, not apparent in the budget at the time that assistance commitments are made. Public housing also entails substantial tax expenditures that arise from the tax-exempt bonds and notes that are issued to finance new projects.

1/ Public housing projects may be newly built or substantially rehabilitated or may be previously existing, standard units purchased for use as public housing. The cost estimates presented in this paper consider only the new construction and acquisition-with-rehabilitation programs, which account for the vast majority of all recent public housing subsidy commitments and are expected to account for all new commitments in the future. The cost estimates appearing here pertain only to the conventional low-rent public housing program and do not consider Indian housing that is developed and financed under different procedures.

This chapter describes the procedures currently used to fund public housing, presents projections of the long-term costs of public housing subsidy commitments made in fiscal year 1980, and compares estimated long-term outlays with the level of funding provided at the outset. Both direct and indirect: costs are examined.

THE NATURE OF DIRECT EXPENDITURES AND CURRENT FUNDING PROCEDURES

For each new unit of public housing provided, the total direct federal expenditure is the sum of the debt-service payments and the annual operating subsidies.

Debt-Service Payments

Public housing projects are financed through tax-exempt bonds and notes issued by the PHAs that develop and own the housing. For each subsidy commitment made, HUD reserves an amount of budget authority assumed to be sufficient to retire the bonds and notes through 40 yearly payments of equal amounts. The eventual federal expenditure required to pay the debt service cost will depend on the per-unit development cost and the terms on the bonds and notes issued to finance development.

Once construction is completed and the financing terms are set, the yearly capital subsidy is known and will be fixed for the life of the assistance commitment. A number of processing stages occur, however, between the initial assistance commitment and the point at which the eventual debt-service cost becomes known. The amount of budget authority reserved when HUD makes a preliminary commitment to fund an additional unit of public housing is based on prototype construction expenses established by HUD for each market area, with financing costs assumed to be those associated with a 40-year mortgage bearing a 6.625 percent annual rate of interest. After initial project approval, the PHA submits a complete development plan with specific cost estimates based on proposed project characteristics. This development plan becomes the basis for an annual contributions contract (ACC) between HUD and the local agency. Costs agreed to in the ACC may differ from the amount estimated at the funds-reservation stage. The ACC is also subject to amendment after construction is completed and the final development cost becomes known.

Annual Operating Subsidies

Annual operating subsidies for PHAs managing public housing projects are calculated on a yearly basis, and funds to pay the subsidies are appropriated in the year in which the expenses are expected to be incurred. The annual subsidy payment for each PHA is determined by a complex set of formulae referred to as the performance funding system (PFS). The PFS establishes an allowable operating expense level for each agency, based on characteristics of the agency's projects, and then separately estimates expected utility costs, rent receipts, and nonrental project income for each PHA. Anticipated project income (rent receipts and nonrental income) is subtracted from the total of the allowable expenses and utility costs to arrive at the subsidy amount.

For each additional unit of public housing, the total operating subsidy requirement over an extended period of time will depend on the initial allowable expense level; initial utility costs; the income of the first tenants, the share of their income that they contribute toward rent, and any non-rental income that the agency can expect to receive; and the rates of increase in allowable operating expenses, utility costs, tenant incomes, and nonrental project income.

THE DETERMINANTS OF DIRECT SUBSIDY COSTS

Debt-Service Costs

For projecting the debt-service costs of future public housing subsidy commitments, data are available on initial assistance commitments made through fiscal year 1978. The average total development cost for commitments made in that year was $40,330 per unit; development costs for different sized units can be estimated (see Table 8). These figures, adjusted to reflect subsequent cost increases, serve as the basis for estimating the development costs of subsidy commitments expected to be entered into in fiscal year 1980. In calculating the corresponding debt-service costs, it has been assumed that all projects will be financed by means of 40-year,

self-liquidating bonds bearing annual interest rates of 6 percent. 2/

TABLE 8. ESTIMATED AVERAGE DEVELOPMENT COST PER UNIT FOR FISCAL YEAR 1978 PUBLIC HOUSING SUBSIDY COMMITMENTS BY SIZE OF UNIT: IN DOLLARS a/

	Number of Bedrooms b/					Average,
	Zero	One	Two	Three	Four or More	All Units
Estimated Development Cost	26,236	30,037	36,541	47,028	51,998	40,330

SOURCE: Derived from HUD management information report.

a/ Figures are for preliminary project approvals. All figures exclude subsidy commitments made under the Indian housing program.

b/ Average development cost for all units is derived directly fron HUD report. Costs for units with different numbers of bedrooms are estimates, based on the ratios of maximum permissible mortgage amounts for different sized units in HUD multifamily mortgage insurance programs.

2/ Until 1974, all new public housing projects were financed through the issuance of long-term bonds. In that year, HUD placed a ceiling of 6 percent on the interest rate that could be paid on such bonds, and since then no new long-term bonds have been issued. For public housing developed since 1974, local agencies have been financing their projects through short-term 3- to 12-month bonds and notes, with new bonds and notes issued as each set becomes due. It is HUD's expectation that long-term financing will eventually be achieved for these projects and that at some time in the future new public housing subsidy commitments will be financed from the outset by long-term instruments.

Initial Operating Subsidy Costs

For estimating initial operating subsidy costs, the latest available data are from fiscal year 1978. The average annual subsidy expected to be paid during that year was approximately $617 for each unit available for occupancy. 3/ This reflects annual total PHA expenses of $1,493 per unit, including allowable operating expenses of $1,001 4/ and utility costs paid by the agency equal to about $492. 5/ These costs are offset by project income equal to about $876 per unit, including $803 from rent payments and $70 from nonrental PHA income. Since each agency's subsidy is based on the characteristics of all of its projects taken together, new units will affect the subsidy payments for all of the existing projects owned by the agency developing the new housing. In most cases, the effect of the new units will be to reduce slightly the subsidies paid to existing projects, because the new housing will lower the average age of a PHA's

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3/ Figures are for those PHAs receiving subsidies under the performance funding system (PFS). The numbers do not reflect the expenses and income of PHAs whose subsidies are calculated separately from the PFS allocation process (Alaska, Guam, Puerto Rico, and the Virgin Islands public housing agencies).

4/ Includes allowable operating expenses set by the PFS and estimated expenses for independent public audits and for other fully-funded expenditures.

5/ Utility costs paid directly by the tenants--estimated to be about $88 per unit per year in fiscal year 1978--appear as neither expenses for the agency nor as receipts from tenants. These direct tenant utility payments lower total project income because they reduce the amount that tenants pay to the PHA.

projects--one of the factors used to establish the agency's allowable expense level. 6/

Utility expenses, rent receipts, and nonrental project income for the new units are assumed to be identical to those values for the existing public housing stock. Tenants in the new units are assumed to have average incomes identical to people currently living in public housing and to pay similar shares of their income toward their own housing expenses. 7/ The average annual family income, before adjustments, of households recertified for continued occupancy in public housing between October 1976 and September 1977 was $4,656 (see Table 9). The average contribution of tenants toward their own housing expenses was slightly greater than 19 percent of unadjusted income. The mix between elderly and nonelderly projects for fiscal year 1978 commitments, which is very heavily weighted toward nonelderly households, is assumed to hold for commitments made during fiscal year 1980.

6/ For public housing commitments made in fiscal year 1980, the additional units are assumed to resemble existing projects in all characteristics, other than age, that affect an agency's allowable expense level. Nine-tenths of all new units are assumed to be distributed among existing agencies in proportion to each PHA's current share of the total public housing inventory; the effect that these new units have on the subsidies paid to existing projects is attributed to the new units alone. The remaining new units are assumed to be built by agencies with no housing currently under management.

7/ Maximum income limits for tenants in public housing are set at levels slightly below those that apply to the Section 8 program. The proportion of income that tenants pay toward rent and utility costs is fixed by the individual public housing agencies but cannot exceed 25 percent of adjusted income. The adjustments to income, the minimum rent payments, and the circumstances under which different rent levels apply all differ between the Section 8 and public housing programs. These differences in rent rules result in a lower tenant contribution rate in public housing.

TABLE 9. AVERAGE INCOME AND AVERAGE PERCENT OF INCOME PAID IN RENT FOR TENANTS RECERTIFIED FOR CONTINUED OCCUPANCY IN PUBLIC HOUSING, OCTOBER 1976 THROUGH SEPTEMBER 1977: BY HOUSEHOLD TYPE

	Nonelderly Headed Households					Elderly Headed Households				
	One Person	Two Persons	Three Persons	Four Persons	Five or More Persons	One Person	Two Persons	Three or Four Persons	Five or More Persons	All Households
Average Income (in dollars)	3,579	4,318	4,985	5,808	6,836	2,829	4,491	5,569	6,839	4,656
Average Percent of Income Paid in Rent a/	23.9	21.6	19.6	17.4	15.7	24.1	17.0	16.0	14.8	19.2
Proportion of all Tenants (in percents)	3.4	9.9	12.3	11.1	19.3	31.0	8.5	2.9	1.6	100.0
Estimated Proportion of all Fiscal Year 1978 Subsidy Commitments (in percents) b/	5.0	14.5	18.0	16.2	28.3	12.6	3.5	1.2	0.7	100.0

SOURCE: HUD management information system report.

a/ Average percent of income paid in rent for each type of household is an estimate derived from HUD data. The average for all households is taken directly from the management information system report.

b/ The estimated distribution among households for fiscal year 1978 commitments is based on the split between elderly and nonelderly units and the expected distribution of households by size within each age group.

Long-Term Operating Subsidy Costs

Operating subsidy payments for new public housing units will increase over time at rates dependent on the rates of increase in allowable operating expenses, utility costs, and project income (which, in turn, depends on the rate of change in tenant incomes). Under the performance funding system, the annual increase in allowable operating expenses for each agency is fixed by HUD and is based on changes in local government wage rates. Projected utility costs for each year are based on prior consumption patterns and expected future utility rate schedules. Rental income is projected annually by each agency based on the latest actual rent collections, increased in accordance with a HUD-provided factor to reflect expected growth in tenant incomes. Project income from sources other than rent receipts is estimated separately by each agency.

The projected long-term costs of fiscal year 1980 public housing subsidy commitments have been calculated under five different sets of assumptions concerning increases in development costs, operating expenses, utility costs, and tenant incomes. 8/ These assumptions--described in the Appendix--parallel the ones used in calculating Section 8 costs. Public housing projects for which initial commitments are made in fiscal year 1980 are assumed to become available for occupancy in fiscal year 1982 and to be fully occupied in fiscal year 1983.

INDIRECT EXPENDITURES

Public housing entails indirect expenses for the federal government in the form of foregone tax revenues from the interest paid on bonds and notes issued to finance new projects. The tax expenditures reported here assume that purchasers of tax-exempt bonds would otherwise have invested in taxable investments with average interest yields of two percentage points greater than the prevailing rate of inflation. The average marginal tax bracket of purchasers of the bonds is assumed to be 35 percent.

8/ All cost estimates assume that project income from sources other than rent receipts will remain a fixed percent of allowable operating expenses.

PROJECTED COSTS

Total Long-Term Expenditures

Less than one-half of the total long-term federal expenditure for new public housing subsidy commitments is funded at the time that the commitments are made. For the five sets of assumptions concerning future program conditions considered here, debt-service expenses--the only component of overall costs that is funded in advance--account for between 27 and 49 percent of total 40-year costs. From 36 to 60 percent of the eventual costs will appear in the budget as annual appropriations for operating subsidies, but are not provided for at the outset. Tax expenditures account for between 13 and 15 percent of total costs. These expenses do not appear as outlays in budget documents and are not specifically attributed to the public housing program in listings of federal tax expenditures.

Under the five scenarios considered, the total of all direct and indirect costs for new public housing subsidy commitments entered into in fiscal year 1980 ranges from $268,400 to $491,000 per unit over the 40 years following initial project occupancy (see Table 10). The debt-service payments do not vary with future economic and programmatic circumstances. Operating subsidy costs and tax expenditures, on the other hand, are sensitive to differences in long-term rates of increase in housing expenses and tenant incomes. Debt-service payments total $130,400 per unit for each of the five cases. The 40-year operating subsidy costs vary from $96,400 to $296,400 per unit. Tax expenditures range from $41,600 to $64,200.

Average Annual Costs

Under the different assumptions considered, the average annual cost, including both direct and indirect expenditures, for each unit of public housing added to the current inventory ranges from $6,710 to $12,280 over 40 years (see Table 11). Expressed in terms of constant (fiscal year 1980) dollars, the average annual cost ranges from $2,420 to $2,740 per unit.

TABLE 10. LONG-TERM COSTS PER UNIT FOR PUBLIC HOUSING SUBSIDY COMMITMENTS ENTERED INTO IN FISCAL YEAR 1980 UNDER VARIOUS ASSUMPTIONS CONCERNING FUTURE INCREASES IN DEVELOPMENT COSTS, OPERATING EXPENSES, UTILITY COSTS, AND TENANT INCOMES: IN DOLLARS a/

Assumption b/	Debt-Service Cost	Operating Subsidy Cost	Tax Expendi-tures	Total Cost
Case 1 (3.9 percent inflation)	130,400	96,400	41,600	268,400
Case 2 (4.7 percent inflation)	130,400	116,000	46,800	293,200
Case 3 (6.1 percent inflation)	130,400	201,000	56,100	387,500
Case 4 (6.1 percent inflation)	130,400	257,400	56,100	443,900
Case 5 (7.3 percent inflation)	130,400	296,400	64,200	491,000

a/ Costs are estimated for the 40 years from the time that a project is fully occupied.

b/ See Appendix for a description of the assumptions used.

TABLE 11. PROJECTED AVERAGE ANNUAL COST PER UNIT FOR PUBLIC HOUSING SUBSIDY COMMITMENTS ENTERED INTO IN FISCAL YEAR 1980 UNDER VARIOUS ASSUMPTIONS CONCERNING FUTURE INCREASES IN DEVELOPMENT COSTS, OPERATING EXPENSES, UTILITY COSTS, AND TENANT INCOMES: IN CURRENT AND CONSTANT DOLLARS a/

	Direct Debt-Service and Operating Subsidy Costs		Total Direct and Indirect Costs c/	
Assumption b/	Average Annual Cost	Cost in Constant (FY 1980) Dollars	Average Annual Cost	Cost in Constant (FY 1980) Dollars
Case 1 (3.9 percent inflation)	5,670	2,270	6,710	2,740
Case 2 (4.7 percent inflation)	6,160	2,120	7,340	2,600
Case 3 (6.1 percent inflation)	8,280	2,050	9,690	2,530
Case 4 (6.1 percent inflation)	9,700	2,250	11,100	2,730
Case 5 (7.3 percent inflation)	10,670	1,940	12,280	2,420

a/ Costs are estimated for the 40 years from the time that a project is fully occupied.

b/ See Appendix for a description of the assumptions used.

CHAPTER IV. REASONS FOR COST DIFFERENCES AND COMPARATIVE PROGRAM COSTS

The cost figures presented in the preceding chapters indicate what the long-term federal expenditure would be for housing assistance commitments made in fiscal year 1980, if current program conditions persist. Because the programs differ with respect to the incomes of the tenants served, however, the figures presented thus far do not indicate what the relative costs of the various programs would be if each served identical households. This chapter discusses the reasons for the differences in program costs and describes what the relative costs would be of aiding the same set of households under each program.

REASONS FOR COST DIFFERENCES

The principal reasons for the cost differences reported in Chapters II and III are:

- Differences in tenant incomes and in the shares of income that tenants pay in rent;
- Differences in the type of housing provided; and
- Differences in the subsidy mechanisms used.

Differences in Tenant Incomes and Rent Payments

Some of the cost differentials among rental assistance programs are the result of differences in tenant incomes and in the shares of income that they are required to pay toward their housing expenses. Because tenant contributions offset federal expenditures, and because all programs tie tenant payments to their incomes, those programs that serve higher-income persons or that require tenants to contribute a greater proportion of their income in rent will be less costly to the government.

The Section 8 existing housing program is currently serving the lowest-income mix of tenants, with the Section 8 new construction/substantial rehabilitation program serving persons with somewhat higher incomes, and the public housing program serving the highest-income mix of tenants. For most types of households, average tenant incomes in Section 8 new construction/substantial rehabilitation projects are actually greater than in public housing, but since the elderly, who tend to have lower incomes, comprise a larger proportion of all the tenants in newly built Section 8 projects, the overall average tenant income is lower than it is in public housing. The very low average income in Section 8 existing housing reflects lower average incomes for most types of households as well. 1/

Tenants in public housing pay a smaller share of their gross income toward rent than tenants in either Section 8 existing housing or new construction/substantial rehabilitation projects. This differential in the proportion of their incomes that families pay in rent--ranging from 19.2 percent of gross income in public housing to 23.5 percent in Section 8 new construction/substantial rehabilitation projects--increases the cost of public housing relative to the cost of the Section 8 program. Some of the difference in average tenant contribution rates between public housing and the Section 8 program can be accounted for by differences in the mix of households served. However, even if the programs were serving identical tenant populations, the average contribution rate would be lower in public housing because of differences in the rules used to define adjusted

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1/ The very low average income in the Section 8 existing housing program also reflects, in part, the tendency of administering agencies to choose tenants from their assisted housing waiting lists. As those lists become depeleted, the average income of tenants in Section 8 existing housing may increase. Many of the currently occupied Section 8 new construction/substantial rehabilitation projects were originally developed by public agencies under other programs and converted to Section 8 use. As more privately sponsored Section 8 new construction/substantial rehabilitation projects become available for occupancy, selectivity on the part of landlords may result in an increase in the average tenant income. If these changes occur, the cost of the Section 8 program would be reduced somewhat relative to the cost of public housing.

income and in the proportion of adjusted income that tenants are required to pay.

Differences in the Types of Housing

The differences in costs between the Section 8 existing housing program and the new construction/substantial rehabilitation programs are attributable primarily to the lower rental costs of existing housing units. For subsidy commitments made in fiscal year 1980, starting Section 8 rents are likely to average about $3,000 per year in existing housing and $5,000 in newly built or substantially rehabilitated projects, making it twice as costly at the outset to assist a typical lower-income household (one that pays about $1,000 per year toward its rent) in a newly built unit as it is to aid the same household in an existing unit. The gap in annual subsidy costs may begin to close in the years following initial occupancy as the newly built projects age and their rents begin more nearly to resemble rental charges in modest existing units.

Differences between the long-term costs of the Section 8 new construction/substantial rehabilitation program and public housing may be accounted for, in part, by differences in development costs. If new housing is constructed in similar locations to serve similar types of households, there is no reason to believe that the particular program for which the housing is built will appreciably affect the cost of construction. It is possible, however, that the absence of explicit development-cost ceilings in the Section 8 program encourages the construction of more expensive projects than are built for public housing. The existing variations in development costs may also result from differences in project locations or in the types of households served (whether small or large families).

Differences in Subsidy Mechanisms

Some of the difference in costs between the Section 8 new construction/substantial rehabilitation program and public housing is the result of differences in the procedures used to finance the individual projects. Because the bonds and notes issued to finance public housing projects are federally guaranteed, they may be offered at lower average rates of interest than the bonds used to finance some of the Section 8 projects. The

lower interest rates mean that the payments made by the federal government to retire the public housing debts will be lower than the debt-service component of Section 8 rents--a cost also paid by the government through annual rental assistance payments.

Differences between the procedure used to make annual rent adjustments in Section 8 new construction/substantial rehabilitation projects and the method used to arrive at yearly increases in allowable operating expenses for public housing also contribute to differences in long-term program costs. Allowable operating expenses in public housing are permitted to increase at a rate equivalent to the increase in local government wages two years earlier; utility costs are permitted to rise at the rate by which utility rate schedules increase. By contrast, owners of Section 8 new construction/substantial rehabilitation projects are granted automatic annual increases meant to compensate them for increases in operating expenses and to keep their rents roughly equivalent to those in comparable, unsubsidized housing. In the past two years, HUD has used two very different methods for determining the automatic rent increases. Last year, rents in occupied Section 8 projects were allowed to rise at the same rate by which rents in all occupied rental units increased. The rent adjustments granted for this year apply the percent increase in rents for all occupied rental housing only to that portion of the rent on a Section 8 unit that is attributable to operating expenses--not to exceed 45 percent of the total rent. The procedure used to calculate the most recent automatic rent adjustments will result in much smaller increases but may also result in a large number of appeals from those owners for whom the automatic adjustment will not cover actual increases in expenses.

The tax preferences that are available to owners of subsidized rental projects increase the costs of the Section 8 new construction/substantial program but do not apply to public housing. Also, because local housing authorities do not pay property taxes on their public housing projects, but instead, make "payments in lieu of taxes" that are generally lower, the expense of managing public housing is reduced relative to the cost of operating comparable privately owned projects.

COMPARATIVE PROGRAM COSTS

Among current rental assistance programs, the Section 8 existing housing program is the least costly to the federal government; of the two new construction programs, public housing is less costly than Section 8. The average annual cost (in constant fiscal year 1980 dollars) of serving a mix of tenants similar to that called for in the latest housing assistance plans, with average incomes comparable to those of persons currently living in newly built Section 8 projects, ranges from $1,560 to $1,750 per unit for the Section 8 existing housing program, depending on the rates of increase in rents and tenant incomes (see Table 12). The average annual constant dollar cost, including both direct and indirect expenditures, of assisting the same households ranges from $2,200 to $2,530 for public housing and from $2,490 to $3,510 for the Section 8 new construction/substantial rehabilitation program.

Depending on the specific set of assumptions made concerning future increases in housing expenses and tenant incomes, the Section 8 existing housing program is from 22 to 35 percent less costly than public housing and from 36 to 50 percent less costly than the Section 8 new construction/substantial rehabilitation program. Because different factors affect the long-term costs of the various programs--marketwide rent increases in the case of the Section 8 existing housing program, increases in the rents of already occupied units for the Section 8 new construction/substantial rehabilitation program, and growth in operating expenses and utility costs for public housing--the ratios among the costs of the different programs vary from one case to another, depending on the ratios among these factors. In every instance, however, the Section 8 existing housing program is the least expensive and the Section 8 new construction/substantial rehabilitation program is the most costly.

The lower cost of the Section 8 existing housing program can be accounted for primarily by the differences in rents between existing and newly built housing. Differences in costs between public housing and the Section 8 new construction/substantial rehabilitation program are caused, in part, by differences in the subsidy mechanisms, as discussed earlier, and may also reflect differences in the quality of the housing or the level of services provided to the tenants. The differences in costs between

TABLE 12. PROJECTED AVERAGE ANNUAL COST PER UNIT FOR FISCAL YEAR 1980 SECTION 8 AND PUBLIC HOUSING SUBSIDY COMMITMENTS ASSUMING IDENTICAL TENANT INCOMES: CONSTANT FISCAL YEAR 1980 DOLLARS a/

Program	Length of Commitment (in years)	Future Increases in Housing Expenses and Tenant Incomes b/ Case 1 (3.9 percent inflation)	Case 2 (4.7 percent inflation)	Case 3 (6.1 percent inflation)	Case 4 (6.1 percent inflation)	Case 5 (7.3 percent inflation)
Section 8 Existing Housing	15	1,640	1,590	1,560	1,750	1,710
Section 8 New Construction/Substantial Rehabilitation	20	2,850	2,750	2,770	3,300	3,110
	30	2,720	2,590	2,610	3,390	3,120
	40	2,660	2,490	2,500	3,510	3,160
Public Housing	40	2,530	2,380	2,320	2,520	2,200

SOURCE: CBO estimates.

a/ Projected costs include both direct subsidy costs and indirect financing subsidies and tax expenditures, as applicable. Assumed average tenant incomes for each program are based on the incomes of present Section 8 new construction/substantial rehabilitation tenants. The assumed tenant mix for each program is 63 percent nonelderly-headed households and 37 percent elderly-headed households.

b/ See Appendix for a description of the assumptions.

public housing and both the Section 8 programs are also, in part, the result of differences in rent rules that permit public housing tenants to count less of their incomes in determining their monthly housing payments. If public housing tenants were charged the same amount for rent that tenants in Section 8 housing are required to pay, the average annual constant dollar cost of public housing would decrease by about 4 percent. Public housing would, however, remain more costly than the Section 8 existing housing program and less expensive than the Section 8 new construction/substantial rehabilitation program.

CHAPTER V. ALTERNATIVE BUDGETARY TREATMENTS FOR HOUSING ASSISTANCE PROGRAMS

At the outset of this paper, two issues were identified regarding the budgetary treatment of lower-income rental assistance programs. The first concerned whether or not the procedures currently used to project long-term budget authority requirements accurately reflect probable program costs. The second concerned what the total direct and indirect costs of the various programs are, and how total costs could be presented in the budget to make them directly comparable across housing programs and more nearly comparable with the costs of nonhousing programs that are not funded in advance. This chapter offers alternative procedures for projecting long-term budget authority requirements and for describing the total direct and indirect costs of assisted housing programs. 1/

PROJECTING LONG-TERM BUDGET AUTHORITY REQUIREMENTS

The Section 8 Program

Although the long-term direct subsidy costs of the Section 8 program depend on numerous factors--the duration of the commitments made, initial rents, initial tenant incomes and the share of their income that they pay toward rent, and the rates by which rents and tenant incomes increase over time--the procedure used to estimate budget authority requirements considers only the length of the commitments and the starting rent levels. The analysis presented in Chapter II indicates that the current procedure may seriously understate actual spending needs, particularly for the lengthier subsidy commitments.

1/ The alternatives presented here are concerned only with estimating and describing long-term program costs. This paper does not address the broader issue of whether housing assistance programs should continue to be advance funded and, if so, how the long-term costs should be financed.

As an alternative to the current procedure for estimating the budget authority requirements of Section 8 assistance commitments, the Congress could direct that, in the future calculations be based on an analysis that explicitly takes into account all of the factors that can affect actual costs. HUD could be required to state in its budget requests not only the assumed duration of commitments and the expected starting rent levels (as they do now), but also the anticipated incomes of Section 8 tenants, the shares of their incomes that they are expected to pay in rent, and the rates by which rents and incomes are assumed to change over time. If the Congress chose, it could employ a different set of assumptions in determining the amount of budget authority to be provided to support new subsidy commitments and could require that HUD use the alternative assumptions in determining the amount of budget authority reserved for each commitment. Depending on the assumptions chosen by the Congress, this could result in either an increase or a decrease in the number of subsidy commitments that could be made.

Under such a scheme, the Congress could be certain that, if specific conditions held in the future, the amount of budget authority set aside for each housing unit would be sufficient to cover long-term costs. Also, if the assumptions made at the outset of each commitment proved to be accurate, there would be less need to use funds provided for the purpose of making new commitments to amend earlier assistance agreements, instead. 2/

Public Housing

Because only the debt-service costs are advance funded, there is less uncertainty concerning the adequacy of the amount of budget authority reserved to finance new subsidy commitments for public housing. However, because one of the principal expenses of public housing--annual operating subsidies--is financed through annual appropriations rather than in advance, the total long-term direct subsidy cost of each additional unit of public housing is necessarily understated at the time that the assistance commitment is made.

2/ Of all the budget authority obligated under the Section 8 program in fiscal year 1978, fully 14 percent was used for cost amendments to contracts entered into in earlier years.

As an alternative to the current budgetary treatment of public housing, the Congress could require that subsequent HUD budget requests include estimates of the eventual operating subsidy expense expected to be incurred for each additional assistance commitment, with the assumptions underlying the estimate made explicit. Including estimates of long-term operating subsidy expenses in the budget would reveal more clearly the full costs, in terms of direct expenditures, of public housing assistance commitments.

DESCRIBING TOTAL PROGRAM COSTS

In addition to requiring that budget proposals include estimates of the long-term direct subsidy costs of new assistance commitments based on an explicit consideration of all the factors that will affect actual expenditures, the Congress could require that future budget documents provide estimates of the total of all direct and indirect costs for new subsidy commitments. Estimates of total program costs, including indirect financing subsidies and foregone revenues as well as direct subsidy expenditures, could be expressed in terms of average annual constant dollar expenses over the lives of the assistance commitments, so that the long-term effects of inflation would be largely factored out. Such estimates would be more comprehensive than any figures currently appearing in the budget and would be more directly comparable across different housing programs. Estimates of average annual constant dollar costs would also be more directly comparable with the annual budget requests for non-housing programs that are not advance funded.

CHAPTER VI. OPTIONS FOR REDUCING PROGRAM COSTS

There are three approaches that the Congress may wish to consider in addressing the funding inadequacies for housing assistance programs that may result from current budgetary practices:

- o Continue current funding practices, with an understanding that additional budget authority may be required in future appropriations to fund insufficiencies from earlier years.

- o Change the present funding procedures, as described in Chapter V, to provide more budget authority when assistance commitments are first made, thereby reducing the likelihood of a shortfall.

- o Reduce the costs of the programs themselves.

This chapter describes a number of options for reducing the long-term costs of housing assistance programs. Some options apply to all programs while others pertain to specific ones. There are potential disadvantages associated with each of the options.

REDUCING OVERALL HOUSING ASSISTANCE COSTS

Options for reducing the costs of all current housing assistance programs include:

- o Increase the reliance on existing housing;

- o Increase the share of income that tenants are required to pay in rent; and

- o Alter the mix of tenants to serve persons with higher incomes.

Increase the Reliance on Existing Housing

Because of the substantial difference in rents between new and existing housing, housing assistance costs could be reduced appreciably by directing a larger share of all housing aid to programs that make use of the existing rental stock. In recent years, however, the trend has been towards less, rather than more, existing housing assistance. In fiscal year 1977, the Section 8 existing housing program and the purchase of existing, standard units for use as public housing accounted for 48 percent of all new subsidy commitments. During the next year, the rate dropped to 45 percent. HUD's original budget submission for fiscal year 1979 called for 41 percent of the additional commitments to be made through the Section 8 existing housing program and for no further direct purchases of existing standard units for public housing. The most recent operating plan for fiscal year 1979 and the HUD budget submission for 1980 call for 34 percent of all commitments to be for Section 8 existing housing. 1/ By shifting the emphasis from new construction to existing housing, more persons could be assisted at a lower total cost to the federal government. Because of the shorter lead time needed to lease existing units, however, a move toward more existing housing assistance would actually increase federal outlays for the first few years after the commitments are made.

Although increasing the reliance on existing housing assistance would reduce long-term costs, it might also diminish the effect of housing assistance programs on the supply of decent housing. Because the Section 8 new construction/substantial rehabilitation program provides an owner with a partial guarantee of rental income, it may encourage the development of housing that would not otherwise have been built. It may, on the other hand, merely substitute subsidized for unsubsidized housing. Since it pays the development and financing costs for publicly owned housing, the public housing program also adds to the supply of new units--provided, again, that the federally financed construction does not merely substitute for development that

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1/ Under current law, HUD is required, as practicable, to provide housing assistance in a manner consistent with needs identified in locally prepared Housing Assistance Plans (HAPs). The trend toward less existing housing assistance reflects, to some degree, a trend in the types of needs identified in the HAPs.

would have occurred in any event. By contrast, the Section 8 existing housing program does not induce new construction. Existing housing assistance does, however, result in some upgrading of marginally substandard units and may contribute to long-term maintenance. It is not clear from available evidence whether the net addition to the supply of decent housing that occurs through new construction programs exceeds the net impact of the upgrading and improved maintenance resulting from existing housing assistance. 2/

Increase Tenant Rent Payments

The Congress could reduce federal outlays by increasing the share of income that tenants in assisted housing are required to pay toward their own housing expenses. For the past ten years, rental charges have been limited by law to no more than 25 percent of adjusted tenant income. The cost of housing assistance programs could be reduced significantly by raising the rental charges to a level above the current standard but still below what tenants would have to pay in the private market for comparable housing. Lower-income renters not receiving housing assistance are now paying an average of 39 percent of their

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2/ If the emphasis in rental assistance programs were shifted toward existing housing, other programs, such as tandem financing assistance, would be available to encourage the production of new, unsubsidized housing at considerably lower per-unit federal costs than the Section 8 new construction/substantial rehabilitation or public housing progams. Even with a fairly high level of tandem financing assistance to the private housing sector, a combination of lower-income, existing-housing rental assistance and tandem financing assistance for unsubsidized construction could involve lower federal expenditures than the current mix of rental assistance programs alone. Also, emphasizing the use of the existing housing stock in subsidized housing programs while providing countercyclical support to the private construction industry through other mechanisms, would allow the federal government to target construction aid during times of slack private development. This would increase the chance that units built with federal aid would add to the total housing stock rather than merely substitute for development that would have occurred in any event.

incomes for housing, 3/ and fewer than one-fourth of all eligible renters now receive federal aid. By raising rent payments in assisted housing, the cost per household could be reduced and the proportion of the eligible population served could be increased, while still providing a substantial subsidy to those receiving aid. To alleviate the hardship that such a change might cause for the lowest-income families a sliding scale of payments could be established, setting a lower rent-to-income standard for the poorest persons, while imposing somewhat higher rates on better-off tenants.

Smaller savings could be achieved by changing the rent rules in public housing to conform to those governing the Section 8 program. Such a change would reduce federal outlays for public housing operating subsidies and eliminate the disparity that now exists in the treatment of public housing and Section 8 tenants.

Alter the Mix of Tenants

A different approach to reduce the costs of rental assistance programs would be to require that they serve a larger number of persons with higher income. Because tenant rent payments in assisted housing are set at fixed percentages of family income, and because rent collections offset federal expenditures, higher average tenant incomes would result in lower costs to the government. With rental charges ranging from 15 to 25 percent of tenant incomes, every increase of $100 in the average annual tenant income would result in a savings to the government of between $15 and $25 per year for each unit of housing.

Increasing the proportion of higher-income tenants would also promote economic integration in assisted housing projects. It should be noted, however, that such economic integration is already encouraged under current law and regulations but has proven difficult to achieve. To the extent that HUD did succeed in shifting the tenant mix toward persons with higher incomes,

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3/ CBO tabulation of the 1976 Annual Housing Survey. Excludes persons paying no cash rent and those living in single-family homes on ten acres or more.

the programs would then serve a greater number of families more likely to be able to afford decent housing in the unsubsidized market, to the exclusion of the lower-income families they would replace.

REDUCING COSTS IN SPECIFIC PROGRAMS

Cost Reductions in the Section 8 Existing Housing Program

Eliminate the Ceiling on Rents. Because Section 8 existing housing tenants are forbidden from renting units costing more than HUD-established maximums, there is continuing pressure to raise the maximum rent schedules in order to expand housing opportunities. This, in turn, increases federal outlays. Although the rent ceilings are intended to hold down subsidy costs, they may, therefore, have the opposite effect. 4/ In some instances, the fair market rent level may even act as a floor, inducing landlords to increase rents up to the FMR when their tenants join the program and to raise rents by the full amount by which FMRs increase each year. 5/

It is possible that federal outlays could be reduced by treating the fair market rent levels as benchmarks for the cost of modest housing but not as maximum allowable rents. Under such a system, the rental assistance payment would be set equal to the difference between the benchmark amount and a fixed proportion of the tenant's income, regardless of the

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4/ Between fiscal years 1977 and 1978, the agreed upon maximum rent levels for new existing housing assistance commitments increased at a rate far in excess of the 7 percent by which rents grew market-wide.

5/ Of a sample of households receiving Section 8 existing housing assistance as of October 1976, 60 percent of those remaining in the same units they were living in before joining the program experienced rent increases at the time that they entered Section 8. Fully 19 percent experienced rent increases of 50 percent or more. (Department of Housing and Urban Development, Lower-Income Housing Assistance Program (Section 8): Interim Findings of Evaluation Research, November 1977.)

actual rent level. Persons would be permitted to rent any unit that met the minimum physical quality standard, paying the full amount in excess of the benchmark rent level themselves and realizing all of the savings from renting below the benchmark amount.

With the fair market rents no longer serving as ceilings, there might be less pressure on HUD to increase allowable rents and, thus, program costs. Fair market rents could be increased at a slower pace without completely closing off segments of the rental market to Section 8 tenants. During periods of rapid inflation in rents, cost increases could be shared between assistance recipients and the government. There would also be a greater incentive for tenants to seek lower-cost housing, because they would save the entire amount of any rent reduction they could realize.

Make Assistance Payments Directly to Tenants. Some cost savings might be realized by having the local housing agencies that administer the Section 8 existing housing program make the assistance payments directly to tenants instead of their landlords. Such a change could reduce administrative expenses by eliminating the need for a contractual relationship between the landlord and the local agency. Under such a procedure, the tenant would be solely responsible for making the rent payment to the landlord.

The agencies administering the Section 8 existing housing program currently spend more than one-tenth of their administrative budgets recruiting landlords and dealing with them on behalf of tenants. 6/ If the agencies made assistance payments directly to the tenants, some portion of this expenditure could be saved and the administrative burden of the program reduced. On the other hand, eliminating the agency-landlord linkage might reduce the ability of the PHAs to aid those people who require assistance in locating and acquiring suitable housing in the private market.

6/ HUD, Lower-Income Housing Assistance Program (Secction 8); Interim Findings of Evaluation Ressearch (November 1977).

Cost Reductions in the Section 8 New Construction/ Substantial Rehabilitation Program

Limit Development Costs. It might be possible to reduce somewhat the cost of Section 8 new construction/substantial rehabilitation assistance by placing limits on the development costs for projects built under the program. Currently, HUD sets maximum rents for Section 8 projects, but does not limit development costs. If the rent ceiling in a particular market is higher than needed to pay the construction, financing, and operating costs of new housing, project owners may be encouraged to build more expensive units, simply because the federal rental guarantee is available. This phenomenon of "building up to the fair market rents" may be exacerbated by the number of parties to the development process whose fees are linked to development costs and who, therefore, have an incentive to increase construction costs.

Although limiting development costs would provide a further cost control, establishing such limits would entail some risks. For one thing, the limitation could result in the construction of lower-quality, less durable housing. Limits on development costs might also discourage participation by private developers.

Change the Procedure for Calculating Annual Rent Increases. By law, HUD is required to adjust rents in occupied Section 8 new construction/substantial rehabilitation projects each year after initial occupancy to cover increased operating costs and to keep Section 8 rents comparable to those in equivalent unsubsidized projects. The current procedure for determining the Section 8 rent adjustments may not, however, accurately reflect rent increases in comparable projects.

The rent adjustments that took effect in November 1977 were based on the average increases in contract rents as determined by consumer prices survey of the Bureau of Labor Statistics. The adjustments reflected increases in rents for all occupied units. Yet, the Section 8 projects to which the increases were applied were all recently built. If the percent increase in rents for all existing units taken together exceeds the percent increase for newly built units, then the November

1977 adjustment factors may have overstated rent increases in unsubsidized housing comparable to the Section 8 projects. 7/

In an attempt to reduce program costs, HUD recently changed the procedure for determining annual Section 8 rent adjustments. Adjustment factors published in January 1979, for effect retroactively to November 1978, applied the percent increase in rents for all occupied units to only that share of the Section 8 rent that is attributable to operating expenses--up to a maximum of 45 percent of the base rent. Thus, if rents went up by 6 percent in a particular market, the automatic adjustment in Section 8 projects would be limited to 2.7 percent (the 6 percent increase applied to 45 percent of the base rent). This procedure will almost certainly not permit rents in Section 8 projects to keep pace with rents in comparable housing and may not even allow owners of Section 8 projects to recover annual cost increases. Strenuous objections to the recently published regulations have already been raised by the owners of Section 8 projects.

If rents in recently completed housing are, in fact, increasing more slowly than rents market-wide--but less slowly than implied by HUD's latest adjustment factors--it might be possible to lower long-term Section 8 costs somewhat from what they would be under the earlier scheme for adjusting rents, while not moving to a system as restrictive as that just implemented. Specifically, yearly Section 8 rent adjustments could be based on average rent increases in newly built housing only, instead of relying on market-wide rent changes as the guide. Alternatively,

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7/ Rent increases in any sector of the market should reflect cost increases and a desire on the part of the owner to maintain a reasonable return on his investment as the value of the property increases. Cost increases alone from one year to the next should reflect almost exclusively increases in operating expenses and utility costs; debt-service costs should increase only for those projects that are refinanced. Operating expenses and utility costs together will be a smaller share of total costs for newly built projects than for all existing rental units taken together. Any increase in operating expenses and utility costs will, therefore, represent a greater percent increase in rents in older existing units than in newly built ones.

HUD could move to an even more restrictive procedure, by basing rent increases on actual growth in costs, requiring project owners to justify yearly adjustments by documenting all cost increases. Such a procedure, however, would run the risk of delaying unduly or denying entirely needed increases, resulting in reduced maintenance and jeopardizing the financial viability of Section 8 projects. Severely constraining annual Section 8 rent increases might also jeopardize the program by inducing project owners to convert their properties to unsubsidized use.

Cost Reductions in Public Housing

Use More Existing Units. Significant savings could be realized in the public housing program by shifting from a near-total reliance on the construction of new units or the substantial rehabilitation of severely dilapidated ones to a greater emphasis on acquiring existing, standard units. A shift toward the purchase of existing units, however, would reduce the impact of the public housing program on the level of residential construction and could also result in less desirable units being made available to public housing tenants.

Alter the Procedure for Determining the Annual Adjustment in Allowable Operating Expenses. Under current procedures, the operating expense base used to calculate annual operating subsidies for PHAs managing public housing is permitted to increase each year at the rate by which local government wages increased two years earlier; increases in non-labor expenses are not taken into account. If the cost of materials rises more slowly than the cost of labor, the current system for adjusting public housing operating expenses will, therefore, overstate actual cost increases. Because the permissible increases are based on the rate of growth in wages from two years earlier, allowable expense increases will also overstate actual growth in costs during periods of declining inflation rates. By changing the procedure for adjusting allowable operating expense levels to take into account more recent wage trends as well as non-labor costs, it might be possible to hold down annual subsidy increases during periods of declining inflation and when material costs are rising more slowly than wages.

APPENDIX

APPENDIX. ASSUMPTIONS USED IN PROGRAM COST PROJECTIONS

The cost projections appearing in this paper apply five different sets of assumptions concerning the rates by which housing expenses (development costs, market rents, operating expenses, and utility costs) and tenant incomes will increase in the future. The five sets of assumptions are based on past trends in housing costs and incomes and cover a range of plausible future circumstances. None of the assumptions should be viewed as predictions of the future, nor should the assumptions employed here be considered to encompass the full set of possible future conditions.

The following five cases are summarized in Table A-1.

Case 1

Increases in housing expenses phase down from current rates to levels consistent with average cost increases occurring between 1957 and 1977. Beginning in five years, tenant wage income increases at the rate by which the average hourly wage grew over that 20-year period; benefit payments to tenants increase at the rate by which the Consumer Price Index (CPI) grew from 1957 to 1977. The underlying post-1983 rate of inflation in this case is 3.9 percent per year.

Housing Expenses. Between now and fiscal year 1984, average gross rents in the Section 8 existing housing program increase at rates consistent with the latest CBO economic projections for those years; beginning in fiscal year 1984, average rents increase at the estimated annual rate by which gross rents grew between 1957 and 1977, including cost increases resulting from the replacement of older, less expensive units with newer, more costly ones. For Section 8 new construction/substantial rehabilitation projects, between now and fiscal year 1980, starting rents increase at a rate corresponding to a combination of the CBO projections for increases in residential construction and gross rents during that period, with each factor counted equally. Following completion of projects in fiscal year 1982,

rents increase at the rate by which gross rents in already occupied units grew between 1957 and 1977. Development costs for public housing increase between now and fiscal year 1980 at a rate consistent with CBO economic projections for that two-year period. Between now and fiscal year 1984, public housing operating expenses increase at the projected rate of growth in average hourly earnings; utility costs increase at rates consistent with CBO economic projections for that period. Beginning in fiscal year 1984, operating expenses increase at the rate by which average hourly earnings grew between 1957 and 1977 and utility costs increase at the rate by which they grew over that twenty-year period.

Tenant Incomes. Between now and fiscal year 1984, tenant income from wages and other non-welfare or benefit sources increases at the projected rate of growth in average hourly earnings; welfare and benefit payments increase at the projected rate of increase in the CPI during that period. Beginning in fiscal year 1984, rates of increase parallel increases in average hourly earnings and in the CPI between 1957 and 1977.

Case 2

Increases in housing expenses phase down from the present rates to levels consistent with average rates of increase between 1962 and 1977. Increases in tenant wage income parallel average hourly wage increases over that 15-year period; benefit and welfare payments increase at the average rate of increase in the CPI. The underlying rate of inflation after 1983 is 4.7 percent annually.

Housing Expenses. Between now and fiscal year 1984, average gross rents in the Section 8 existing housing program increase at rates consistent with the latest CBO economic projections for those years; beginning in fiscal year 1984, rents grow at the estimated annual rate by which gross rents increased between 1962 and 1977, including cost increases resulting from the replacement of older, less expensive units with newer, more costly ones. For Section 8 new construction/substantial rehabilitation projects, between now and fiscal year 1980, starting rents increase at the rate assumed in Case 1. Following completion of projects in fiscal year 1982, rents increase at the rate by which rents in already occupied units grew between 1962 and 1977. Development costs for public housing increase between now

and fiscal year 1980 as described in Case 1. Between now and fiscal year 1984, public housing operating expenses increase at the projected rate of growth in average hourly earnings, and utility costs increase at rates consistent with CBO economic projections for that period. Beginning in fiscal year 1984, operating expenses increase at the rate by which average hourly earnings grew between 1962 and 1977; utility costs increase at the rate by which they grew over that same period.

Tenant Incomes. Between now and fiscal year 1984, wage and other non-welfare or benefit income increases at the projected rate of growth in average hourly earnings; welfare and benefit payments increase at the projected rate of increase in the CPI during that period. Beginning in fiscal year 1984, increases parallel growth in average hourly earnings and the CPI between 1962 and 1977.

Case 3

Increases in housing expenses phase down from current rates to levels consistent with average cost increases occurring between 1967 and 1977. Beginning in five years, tenant wage income increases at the rate by which average hourly earnings grew between 1967 and 1977 and benefit and welfare payments to tenants increase at the rate by which the CPI grew over those ten years. The underlying rate of inflation after 1983 is 6.1 percent per year.

Housing Expenses. Between now and fiscal year 1984, average gross rents in the Section 8 existing housing program increase at rates consistent with the latest CBO economic projections for those years; beginning in fiscal year 1984, average rents increase at the estimated annual rate by which gross rents increased between 1967 and 1977, including cost increases resulting from the replacement of older, less expensive units with newer, more costly ones. Starting rents in Section 8 new construction/substantial rehabilitation projects increase in the manner described in Case 1. Following completion of projects in fiscal year 1982, rents increase at the rate by which rents in already occupied units grew between 1967 and 1977. Development costs for public housing increase between now and fiscal year 1980 at the same rate as in Case 1. Between now and fiscal year 1984, public housing operating expenses increase at the projected rate of growth in average hourly earnings and utility costs increase at rates consistent with CBO economic projections for

that period. Beginning in fiscal year 1984, operating expenses increase at the rate by which average hourly earnings grew between 1967 and 1977; utility costs increase at the rate by which they grew over that ten-year period.

Tenant Incomes. Between now and fiscal year 1984, wage and other non-welfare or benefit income increases at the projected rate of growth in average hourly earnings; welfare and benefit payments increase at the projected rate of increase in the CPI during that period. Beginning in fiscal year 1984, income growth parallels the increases in average hourly earnings and the CPI between 1967 and 1977.

Case 4

Increases in housing expenses phase down from present rates to levels below current rates but somewhat greater than the steady-state level assumed in Case 3. Tenant income increases at rates slightly greater than those in Case 3. The underlying rate of inflation after 1983 is 6.1 percent per year.

Housing Expenses. Between now and fiscal year 1984, average gross rents in the Section 8 existing housing program increase at rates consistent with the latest CBO economic projections for those years; beginning in fiscal year 1984, the projected rate of increase for that year holds. For Section 8 new construction/substantial rehabilitation projects, between fiscal years 1978 and 1980, starting rents increase at the same rates assumed for Case 1. Between fiscal years 1982 and 1984, rents in occupied Section 8 new construction/substantial rehabilitation projects increase at the projected rate of growth in rents for already occupied housing; following 1984, the projected rate of increase for that year holds. Development costs for public housing increase in the manner described in Case 1. Between now and fiscal year 1984, public housing operating expenses increase at the projected rate of increase in average hourly earnings, and utility costs increase at rates consistent with CBO economic projections; thereafter, the rates of increase projected for that year continues.

Tenant Incomes. Tenant income from wages and other non-benefit and welfare sources increases at the rate by which average hourly earnings are projected to increase through fiscal year 1984, with the rate of increase for 1984 continuing thereafter. Benefit and welfare income increases at the projected rate of increase in the CPI.

Case 5

Housing expenses and tenant incomes increase at annual rates consistent with CBO economic projections through fiscal year 1981; the projected rates of increase for that year continue thereafter. This represents a more rapid increase in housing expenses and in tenant incomes than any of the preceding cases. The underlying rate of inflation after 1980 is 7.3 percent.

Housing Expenses. Average gross rents in the Section 8 existing housing program increase at an annual rate consistent with CBO economic projections through fiscal year 1981. For Section 8 new construction/substantial rehabilitation projects, between now and fiscal year 1980, starting rents increase at an annual rate consistent with the projected cost increases for that two-year period, as described in Case 1. Following completion of projects, rents increase at the projected rate of increase in rents for already occupied housing in fiscal year 1981. Development costs for public housing increase between now and fiscal year 1980 at a rate consistent with projected increases in development: costs for that two-year period. Public housing operating expenses increase at the projected rate of increase in average hourly earnings, and utility costs grow at the projected rate of increase for fiscal year 1981.

Tenant Incomes. Through fiscal year 1981, tenant income from sources other than welfare and benefit payments increases at the projected rate of increase in average hourly earnings, and tenant income from welfare and benefit payments increases at the projected rate of increase in the CPI. Thereafter, the rates of increase for 1981 persist.

TABLE A-1. ANNUAL RATES OF INCREASE IN HOUSING EXPENSES AND TENANT INCOMES ASSUMED FOR PROJECTING LONG-TERM HOUSING ASSISTANCE PROGRAM COSTS: IN PERCENTS, BY FISCAL YEAR a/

	1979	1980	1981	1982	1983	1984 and thereafter
CASE 1						
Increase in Housing Expenses						
Gross rents in Section 8 existing housing	7.9	8.2	7.7	7.2	5.6	3.8
Starting rents in Section 8 new construc./sub. rehab. projects	9.4	8.4	—	—	—	—
Annual rents in occupied Section 8 new construc./ sub. rehab. projects	—	—	—	—	4.9	3.1
Public housing development costs	11.7	9.4	—	—	—	—
Public housing operating expenses	6.0	8.2	8.0	8.3	7.1	5.3
Public housing utility costs	7.4	9.8	8.9	8.1	7.3	4.1
Increase in Tenant Income b/						
Wages	7.6	8.2	8.0	8.3	7.1	5.3
Benefits	8.6	8.0	7.3	6.7	6.1	3.9

(Continued)

TABLE A-1. (Continued)

	1979	1980	1981	1982	1983	1984 and thereafter
			CASE 2			
Increase in Housing Expenses						
Gross rents in Section 8 existing housing	7.9	8.2	7.7	7.2	5.6	4.3
Starting rents in Section 8 new construc./sub. rehab. projects	9.4	8.4	--	--	--	--
Annual rents in occupied Section 8 new construc./ sub. rehab. projects	–	–	–	–	4.9	3.6
Public housing development costs	11.7	9.4	–	–	–	–
Public housing operating expenses	6.0	8.2	8.0	8.3	7.1	5.9
Public housing utility costs	7.4	9.8	8.9	8.1	7.3	5.0
Increase in Tenant Income b/						
Wages	7.6	8.2	8.0	8.3	7.1	5.9
Benefits	8.6	8.0	7.3	6.7	6.1	4.7

(Continued)

TABLE A-1. (Continued)

	1979	1980	1981	1982	1983	1984 and thereafter
			CASE 3			
Increase in Housing Expenses						
Gross rents in Section 8 existing housing	7.9	8.2	7.7	7.2	7.1	5.6
Starting rents in Section 8 new construc./sub. rehab. projects	9.4	8.4	—	—	—	—
Annual rents in occupied Section 8 new construc./ sub. rehab. projects	—	—	—	—	6.4	4.9
Public housing development costs	11.7	9.4	—	—	—	—
Public housing operating expenses	6.0	8.2	8.0	8.3	8.1	7.1
Public housing utility costs	7.4	9.8	8.9	8.1	8.1	7.3
Increase in Tenant Income b/						
Wages	7.6	8.2	8.0	8.3	7.1	7.1
Benefits	8.6	8.0	7.3	6.7	6.5	6.1

(Continued)

TABLE A-1. (Continued)

	1979	1980	1981	1982	1983	1984 and thereafter
			CASE 4			
Increase in Housing Expenses						
Gross rents in Section 8 existing housing	7.9	8.2	7.7	7.2	7.1	6.9
Starting rents in Section 8 new construc./sub. rehab. projects	9.4	8.4	—	—	—	—
Annual rents in occupied Section 8 new construc./ sub. rehab. projects	—	—	—	—	6.4	6.3
Public housing development costs	11.7	9.4	—	—	—	—
Public housing operating expenses	6.0	8.2	8.0	8.3	8.1	7.5
Public housing utility costs	7.4	9.8	8.9	8.1	8.1	8.1
Increase in Tenant Income b/						
Wages	7.6	8.2	8.0	8.3	8.1	7.5
Benefits	8.6	8.0	7.3	6.7	6.5	6.1

(Continued)

TABLE A-1. (Continued)

	1979	1980	1981	1982	1983	1984 and thereafter
			CASE 5			
Increase in Housing Expenses						
Gross rents in Section 8 existing housing	7.9	8.2	7.7	7.7	7.7	7.7
Starting rents in Section 8 new construc./sub. rehab. projects	9.4	8.4	—	—	—	—
Annual rents in occupied Section 8 new construc./ sub. rehab. projects	—	—	—	—	7.0	7.0
Public housing development costs	11.7	9.4	—	—	—	—
Public housing operating expenses	6.0	8.2	8.0	8.0	8.0	8.0
Public housing utility costs	7.4	9.8	8.9	8.9	8.9	8.9
Increase in Tenant Income b/						
Wages	7.6	8.2	8.0	8.0	8.0	8.0
Benefits	8.6	8.0	7.3	7.3	7.3	7.3

a/ All figures are expressed as increases from the prior fiscal year.

b/ "Wages" include all income from sources other than public assistance and retirement benefits. "Benefits" include all income from public assistance and retirement benefits.