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Domestic Housing And Community Development

Issues For Planning

A decent, safe, and sanitary home and a suitable living environment for all Americans is a goal that is still far from being achieved. The increasing cost of constructing and operating housing continues to adversely affect our Nation's efforts in meeting housing needs. Likewise, the migration of people and jobs and the increasing cost of providing essential community services has placed many communities in a serious financial position. Whether these problems can be successfully dealt with are major questions to be answered in the s ahead.

study examines current and emerging issues relating to Federal involvement in the sing and community development area and represents the perspective used in organizing audit efforts.

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FOREWORD

Two issues--high housing costs and economically distressed cities--have surfaced as the major concerns facing our Nation over the next few years. Additionally, the Nation will continue to have problems:

--providing and maintaining housing for low-and moderate-income families,

--preserving our existing housing stock and neighborhoods,

--insuring adequate mortgage credit for home buyers and maintaining a viable housing industry,

--assisting economic development in communities through improved public facilities, and

--providing credit to businesses to maintain and improve economic conditions in communities.

This report identifies and describes what we believe are the critical housing and community development issues facing the Nation. This report, in its original form, was prepared as an internal guide to focus our work efforts in the housing and community development area.

We hope that others will find this report helpful in their own activities and that it will foster a better understanding of the crucial issues facing the Nation relating to domestic housing and community development activities.

This study was developed by the Community and Economic Development Division with the cooperation of and input from other divisions and offices. Questions regarding the study should be directed to Ronnie E. Wood, Housing and Community Development Coordinator on (202/426-1630).

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Director, Community and
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CHAPTER 1

OVERVIEW OF ISSUE AREA

Housing and community development problems confronting our Nation are many and varied. Federal efforts to meet the national goal of a decent home and a suitable living environment for every American family involve highly complex interrelationships between economic and social phenomena in both urban and rural communities.

DELINEATION OF THE ISSUE AREA

This issue area encompasses two closely related subjects: one--housing--which is relatively easy to define, and the other--community development--which is more complex and overlaps a number of issue areas. Housing includes:

--Federal programs and activities (mortgage insurance and guarantees, direct loans, grants, and cash subsidies, or other funding relating to (1) the production of new homeownership and rental housing; (2) the preservation of existing homeownership and rental housing through repair work, substantial rehabilitation, or code enforcement action; (3) the rental of decent single-family or multifamily properties; (4) the management and operation of of federally supported housing properties; (5) the management of single-family and multifamily properties acquired through mortgage defaults; (6) the construction, management, and operation of domestic military housing for military personnel and their families; and (7) housing provided by Federal agencies to employees and their dependents).

--Federally sponsored mortgage market activities of the Federal National Mortgage Association, the Federal Home Loan Mortgage Corporation, the Government National Mortgage Association, and the Federal Home Loan Banks.

The delineation of community development programs and activities, as previously noted, is more complex. Many Federal programs impact in some way on the development of a community--the Catalog of Federal Domestic Assistance lists 269. Our interest in this area, however, deals with those programs which affect the community as a whole and its economic development. Our definition of community development therefore includes:

--area and regional development programs,

--Federal efforts designed to make a community a more suitable place to live including Federal programs and activities designed to:

(1) assist communities in preventing and eliminating blight and deterioration,

(2) assist economically distressed communities,

(3) encourage and foster economic development in communities through improved public facilities and through loans and grants to businesses, to the extent these activities' primary focus is on community development, and

(4) minimize the adverse effects from natural catastrophes such as floods, hurricanes and earthquakes.

--evaluation of the significant impact on families, businesses, and communities from the termination, initiation, or major change in Federal installations of programs.

State and local programs frequently supplement or complement Federal programs and have a definite impact on the benefits to be derived from Federal efforts. Therefore, assignments undertaken should also consider State and local activities.

FEDERAL ROLE IN HOUSING AND COMMUNITY DEVELOPMENT PROGRAMS

The history of the Federal role in housing and community development from 1932 to present is intricate and tangled. There are three broad areas of concern that have guided Government actions in the housing and community development activities: the recognition that it had (1) a responsibility to maintain and promote economic stability, (2) a social obligation to help provide for those in need, and (3) an emerging interest in how the Nation's communities developed.

Housing Programs:

In the 1930s the Congress made two fundamental policy decisions which basically remain intact to this day. The first was the complete restructuring of the private home financing

system through the creation of the Federal Housing Administration (mortgage insurance); the Federal Home Loan Bank Board and Bank System (savings and loan industry); institutions like the Federal Deposit Insurance Corporation and the Federal Savings and Loan Insurance Corporation (insurance on deposits of commercial banks, mutual savings banks, and savings and loan associations); and finally the Federal National Mortgage Association, the Government National Mortgage Association, and the Federal Home Loan Mortgage Corporation (secondary mortgage market). Creation of these institutions, resulting in the acceptability of the long-term, low downpayment, fully amortizing mortgage and a system to provide a large flow of capital into the mortgage market, are probably the most significant achievements of the Federal Government in the housing area.

The other fundamental policy decision in the same decade was the concept of government-subsidized housing for low-income families. Although the public housing program authorized in 1937 was intended primarily as a means of stimulating employment and clearing slums, it nonetheless marked the first time that Federal funds were used to finance new housing construction for the less fortunate.

In the years that followed, numerous Federal housing and community development programs were added to the statute books spurred by the 1949 enactment of the national goal of "a decent home and a suitable living environment for every American family." A number of mortgage insurance programs conferring special benefits on such groups as veterans, farmers, the elderly, and those displaced by other Government programs were added. Those programs were, in turn, followed by new subsidized mortgage insurance and subsidized direct loan programs benefiting the elderly, the poor, and the near-poor.

The principal Federal sources of housing assistance are the:

--Department of Housing and Urban Development,

--Farmers Home Administration, Department of Agriculture,

--Bureau of Indian Affairs, Department of the Interior,

--Veterans Administration,

--Department of Defense,

--Federal National Mortgage Corporation,

--Federal Home Loan Mortgage Corporation, and

--Federal Home Loan Banks.

At March 31, 1978, the Federal Government had outstanding insured or guaranteed housing mortgages and home loans totaling $189 billion. For fiscal year 1979 the cash outlay for subsidy payments under various subsidized housing programs will amount to about $4 billion.

The Federal Government's impact on housing is not limited to those types of housing assistance previously mentioned. There are a number of Federal agencies, including the Department of Defense (DOD), that provide housing for their personnel and dependents. DOD, for example, owns and controls 376,000 family housing units, 101,000 bachelor officer units, and 1,000,000 enlisted personnel spaces.

Community Development Programs:

The Government's concern over community growth and development and what the cumulative effects of growth patterns would be on the welfare of the Nation as a whole has been expressed many times and in many forms. Public housing originated in 1937 as an effort to clear slums. Then in 1949 the Congress authorized a major program apart from the public housing program to deal with slum clearance. Still later, starting in 1954 and continuing in the 1960's and early 1970's, the concern over community growth and development was steadily expanded to embrace ever-larger areas: first entire neighborhoods, then whole sections of cities, and finally entire cities and counties and preplanned new communities. These efforts were designed to assist cities to solve urban problems and to encourage them to develop more orderly, attractive, and livable communities.

The Housing and Community Development Act of 1974 significantly affected Federal involvement in community development and housing improvement by replacing programs characterized by narrow, rigid purposes with block grants. Block grant enables a community to initiate efforts addressed to its unique circumstances in order to eliminate slums and blight, conserve and expand the housing stock, increase public services, improve the use of the land, and achieve other desirable community and national growth objectives. One of the important objectives of the act is to reduce the concentrations of lower income persons in impacted areas.

In the area of economic development in communities, the Area Redevelopment Administration (ARA) was established in 1961 to improve the basic infrastructure of rural areas and to provide incentives to businesses to locate in depressed rural areas. In 1965 the Economic Development Administration assumed the earlier purpose of ARA and began to focus economic development to urban areas as well as rural areas.

The Public Works Employment Act of 1976 (P.L. 94-369) was enacted in July 1976. A total of $3.7 billion was initially appropriated to carry out the act. Subsequently an additional $6.25 billion was appropriated to carry out the act. Its major provisions are:

--Title I authorizes financial assistance to State and local governments for local public works projects. Commerce's Economic Development Administration (EDA) was appropriated $6 billion to administer this program.

--Title II is designed to help State and local governments maintain basic governmental services that may not otherwise be available at adequate levels during economic recessions. Treasury's Office of Revenue Sharing was appropriated $3.45 billion for this title.

--Title III authorizes the construction of sewage treatment facilities under the Water Pollution Control Act. The Environmental Protection Agency was appropriated $480 million for this title.

On March 27, 1978, the President released the broad principals and guidelines of his new proposed National Urban Policy. This is an attempt to address the many social and economic problems that have been created by the urban changes and regional shifts of the last two decades--in particular, the dramatic population shifts south and west-ward and the center city decline of the 1970's.

The urban/regional dimension to domestic issues has come suddenly and dramatically to the forefront of recent policy debates. Until recently, the regional issue was perceived as one of rural decline and of underdevelopment of the South. Metropolitan areas of the North were still perceived as the wealthier and dominant regions and areas of the country. In addition, problems of fiscal distress of cities and high unemployment rates, among others, were viewed and dealt with separately and primarily as short-term effects of cyclical downturns in the national economy.

In the last 2 years, however, the severe distress and blight of center cities and their residents have become ever more apparent. Problems such as fiscal and economic health of cities (most notable New York City), high unemployment, recession in such industries as steel and shoes, and inequalities in the distribution of income and social structures are now viewed by many as stemming from a common underlying phenomenon of long-term urban decline.

The public and the policy community, as yet, are still in a state of some disarray on the urban/regional issue. The focus of the problem has shifted both from concerns about rural underdevelopment to concerns about urban decline and from dynamics of cyclical distress to dynamics of long-run secular decline. Nevertheless, the facts, issues and tradeoffs have not yet been sorted out, and much of the debate and media presentation is still reflecting local or regional biases. Also, the causes and consequences of such shifts for cities and for the country at large have been only superficially analyzed by the research and government community. Finally, the public and the policy community have not advanced far in the necessary debate over options and the resolution of conflicts among possible objectives for the cities and for sub-national development in this country.

The principal Federal sources of community development assistance are the:

--Department of Housing and Urban Development;

--Economic Development Administration and the Office of Minority Business Enterprise, Department of Commerce;

--Small Business Administration;

--Farmers Home Administration and Rural Electrification Administration, Department of Agriculture;

--Community Services Administration.

Assistance provided by these agencies include community development block grants, rural electric and telephone loans, business and industrial development loans, planning and research grants, public works loans and grants, and direct or guaranteed loans and subsidies to Indian communities. For fiscal year 1979, expenditures for community and regional development activities will be about $9 billion.

PERSPECTIVE ON CURRENT AND FUTURE HOUSING AND COMMUNITY DEVELOPMENT ISSUES

American society has always been dynamic. Movements of people across the continent, from farm to town or from city to suburb, have marked every era of American history. Americans began moving from densely built up cities to suburban neighborhoods earlier in this century. This trend toward "thinning out" accelerated in the 1950's and 1960's. Then in early 1970's, it was joined by a growing movement of people from the northeastern and north central parts of the country to the south and west. Now population is shifting increasingly to rural areas. In effect, the whole country is thinning out.

Cities are confronted with the need to satisfy rapidly growing expenditure requirements arising from the higher percentage of remaining "high cost" citizens - the poor and the elderly. On the other hand, their tax resources are either declining or are increasing at a decreasing rate, reflecting the exodus of industry and middle- and-high-income families to the suburbs or rural areas.

There is no single reason for this thinning out process. Americans are more mobile today than in the past. People seek better climates and better environments. They also seek to escape pollution and increased crime. New technology, interstate highways, modern airports, and improved communications make it possible for business and industry to locate in the open spaces of undeveloped or less developed areas.

Recent national economic problems have helped to push these migration trends along. High unemployment, high rates of inflation and two recessions marked the first half of the 1970's. Recession struck the northeast and north central regions hardest of all because of their heavier dependence on manufacturing. It heightened the long-term economic decline of both regions and worsened their respective competitive economic positions. Almost all the manufacturing jobs lost in the Nation (1.5 million) between 1970-75 were lost in these two regions.

A highlight of some of the more important activities and issues that will influence future Federal housing and community development policies and programs include:

--30 million increase in population over the next 20 years,

--changing life styles of Americans and increasing preference for one person households. This has occurred because of:

- later marrying ages among young people,
- increased divorces,
- increased longevity of older people, and
- people simply choosing to live alone.

--migration of people and industry to the South and West leaving behind many distressed communities. Recent population and employment changes by region follows:

Population change:

Region	Population Increase 1960-1970 (Percent)	1970-1975 (Percent)
Northeast	9.8	0.8
North Central	9.6	1.9
South	14.3	8.4
West	24.2	8.7
U.S. Total	13.4	4.8

Employment change:

Region	Regional Growth Share of Total Employment Change Percentage 1965-1970	1970-1975
Northeast	20.7	-0.6
North Central	27.2	14.7
South	33.9	55.8
West	18.2	30.1
U.S. Total	100.0	100.0

--rapidly rising housing costs caused by inflation, government regulations and interest rates,

- median sales price of new homes has risen from $23,400 in 1970 to over $63,000 in May 1978. There has been a 16 percent price increase since May 1977,

- average price for existing homes rose to $54,800 in May 1978 for a 17 percent increase over the price in May 1977,

- only 12 percent of all families in 1977 were able to afford (on the basis of family income) a median priced new house,

- examples of 1 year increases (from May 1977 to May 1978) in selected building materials are:

	Percent of increases
-lumber	20
-millwork	30
-gypsum	30
-insulation	10
-ready-mix concrete	14
-brick	15
-asphalt roofing	22

- total homeownership costs increased about 200 percent from 1965 to 1976. For example, property taxes rose 350 percent and utilities about 120 percent during this period, and

- mortgage interest rates over 10 percent for both new and existing housing.

--National housing vacancy rate of 5 percent which is the lowest in over 30 years.

--About 250 of our cities are economically distressed. Federal interest in long-term strategies for central city revival and self-sufficiency will intensify.

The various changes described previously will require greater Federal involvement in future housing and community development policies and programs. Federal efforts will have to deal with:

--the need for over 2 million new housing starts each year to meet our growing and mobile population and emerging lifestyle changes.

--the need to slow down the rapid increases in the cost to construct, operate, and finance housing,

--the increased need to provide housing for lower income persons. Housing deprivation is changing from a problem of physical inadequacies to that of excessive cost,

--the need to preserve our existing housing stock because it is unlikely the construction industry can meet our future housing needs through new construction,

--providing immediate assistance to the most troubled cities and communities. This should be geared to help cities restructure their economies and better adapt to change,

--helping all cities offer their residents decent services, adequate jobs, sound neighborhoods, good housing and healthy environments.

Some recurring housing policy issues facing the Congress include:

--what level of funding should be provided for housing assistance programs and how should they be financed,

--what should be the mix of new construction, rehabilitation, and existing housing assistance,

--what kind of housing assistance should be provided to lower income homeowners, and should direct assistance be extended to higher income families,

--what mix of programs is most effective in encouraging housing production and providing countercyclical aid to the home building industry, and

--how should housing assistance programs be used to encourage community development.

The basic continuing community development problems facing the Congress include:

--the presence of disorderly, uneconomic, and anti-social patterns of development and land use in the Nation,

--increasing fiscal and political fragmentation resulting in an aggravating mismatch of needs and resources,

--the lag in development of community facilities in rural areas and areas experiencing rapid growth,

--citizen alienation and/or apathy in the face of ineffective governmental action, and

--increasingly doubtful viability of many local units of government because of their inability to deal with today's complex problems.

LEGISLATION IMPACTING ON ISSUE AREA

In each session of the Congress over 1,000 individual pieces of legislation impacting on the housing and community development area are introduced. Congressional and executive actions relating to the proposed Urban Policy, Small Business Administration and the consolidation of emergency preparedness and response activities into a single agency could have significant impact on the issue area. The proposed Urban Policy legislation, the amendments to the Small Business Administration, and the consolidation of emergency preparedness and response activities are discussed below.

National Urban Policy

On March 27, 1978, the President released the broad principles and guidelines of his proposed National Urban Policy. The new policy was estimated to require or contain:

--160 plus changes in 38 existing Federal programs to target them more to urban needs,

--30 components requiring new legislation, with an increase of $4.4 billion in the fiscal year 1979 budget, and

--$1.7 billion in tax credits to businesses to encourage relocation in depressed areas.

Legislation includes numerous urban lending proposals such as a National Development Bank and an Urban Lending Act that would require Savings and Loan Associations to invest in community development areas. Consideration of the major urban policy proposals was postponed by the Congrss until 1979.

During August 1978, the President signed four urban policy executive orders. They establish an urban policy impact analysis process, target Federal procurement to labor surplus areas, give preference to urban areas in locating Federal facilities, and legitimize the interagency coordinating council which had been in operation.

Small Business Administration

Small Business Administration legislation was amended in 1978 by P.L. 95-507 and it significantly impacts on our future work. P.L. 95-507 requires GAO to evaluate and report by January 1, 1981, on four SBA programs: economic opportunity loan program; 8(a) procurement program; management assistance to minority businesses; and a new minority subcontracting program. GAO is required also to evaluate and report by June 30, 1980, on two pilot projects. The first involves the waiving of Federal bonding requirements for firms under the 8(a) procurement program and the second involves a project for one executive agency to develop new methods for negotiating contracts for the 8(a) procurement program. The Congress also passed H.R. 11445, a bill which would authorize SBA to make grants to State and regional associations to fund small business development. This bill was vetoed by the President.

Emergency preparedness and response

In September 1978 the Federal Emergency Management Agency was established to consolidate the following emergency preparedness and response activities:

--Federal Preparedness Agency, located in GSA, is concerned with contingency planning for Federal, State and local government, industrial mobilization, and management of limited resources.

--Defense Civil Preparedness Agency, located in DOD, administers civil defense program.

--Federal Disaster Assistance Administration, located in HUD, coordinates Federal natural disaster relief activities and programs and provides funds to States for natural disaster planning.

--Emergency weather warning systems,

--National Fire Prevention and Control Administration,

--National Flood Insurance Program, and

--Office of Earthquake Hazard Reduction.

The new agency is expected to be operational on or about April 1, 1979.

CHAPTER 2

AREAS OF CONCERN

We have identified 19 areas of concern as meriting GAO's attention within the next 18 months if we had unlimited staffing resources. However, since our staffing is limited we have designated the first 8 as priority areas where we will direct most of our audit effort. A detailed discussion of the priority areas is presented in Chapter 3.

PRIORITY:

Housing Related:

1. Evaluation of the Nation's efforts to house lower-income families

2. Minimizing subsidized housing operating costs and improving its management

3. Evaluation of Federal efforts to encourage the production of non-subsidized housing

4. Evaluation of Federal efforts to minimize foreclosures and improve the disposition of acquired properties

5. Assessment of the decisionmaking process for developing housing strategies

Community Development Related:

6. Assisting urban communities to prevent and eliminate blight and deterioration

7. Assisting community development through loans and grants to businesses

8. Assessment of efforts to assist economically distressed communities

NON-PRIORITY:

Housing Related:

9. Effectiveness of Federal efforts to provide and operate military housing

This area involves the effectiveness of the Department of Defense (DOD) in providing, operating, and maintaining military housing. Military family housing is an expensive and valuable investment which requires about $1 billion annually to operate and maintain. Our past work has concentrated on evaluating the need for additional onbase housing at selected military installations and identifying how the military can make greater use of community housing.

GAO AUDIT REPORTS: January 1977 - December 1978

Mortgage insurance premiums paid by DOD for Capehart and Wherry housing, (CED-78-14, 12/12/77); (CED-78-146 and 147, 8/3/78)

Military services are constructing unneeded housing, (CED-78-8, 12/29/77)

Mandatory participation in the DOD self-help program can reduce operation and maintenance costs, (CED-78-26, 1/13/78)

Analysis of the need for additional family housing at the Navy's Trident Submarine Base, (CED-78-49, 2/9/78)

Savings possible through further design standardization of bachelor enlisted quarters (LCD-78-311, 3/9/78)

Is there a need for additional family housing at Fort Stewart? (CED-78-108, 6/7/78)

10. Effectiveness of Federal efforts to eliminate substandard housing

In consonance with the national goal of a decent home and suitable living environment for every American family, the Federal Government should be taking strides to inventory the Nation's substandard housing and to find means by which such housing can be replaced with standard units. Work in this area would evaluate the extent and effectiveness of Federal efforts along these lines.

11. Evaluation of Federal tax laws and their impact on the economy and housing industry

Work in this area would focus on measuring the often hidden cost to the Federal Government inherent in tax laws applicable to housing production, particularly subsidized housing, and assessing the contribution made by such costs to housing production.

12. Financial problems in cities and their impact on Federal housing and community development programs

Many communities are experiencing financial problems. Work in this area will evaluate the actions taken by these communities to alleviate or reduce their financial problems and the impact of these actions on housing production and the provision of public facilities and related services.

13. Evaluation of Federal research and development efforts in housing

Rapid change in housing technology has been inhibited in part by the inability to test or "prove" new ideas easily. There is great reluctance on the part of builders and housing manufacturers to experiment with new products and techniques, since innovations are perceived to be risky under many market conditions. Also the existence of a vast number of divergent and restrictive State and local building codes has slowed growth in housing technology. New products, techniques, and material applications not only produce time and cost savings, but may be of superior quality. How rapidly the industry develops and uses new technology depends among other things on the extent to which new modes of construction are properly tested and, equally as important, on the speed at which innovations can be brought into use through approval by governmental authorities.

14. Evaluation of Federal efforts to simplify housing and community development programs

HUD had 83 housing programs which were active from 1968 to 1978. In addition, the Farmers Home Administration and the Veterans Administration have numerous programs to remedy housing problems of their constituents. The diversity of the Federal Government's interest in housing places some limits on the extent to which its role can be simplified. Work in this area would focus on whether (1) there are problems in the way these programs interrelate and are delivered, and (2) whether the complexities of administrating so many programs prevent progress toward our National housing goals.

Community Development Related:

15. Minimizing the adverse effects on communities from natural catastrophes

Included are Federal efforts to prevent or minimize property damage and loss of life from natural hazards such as floods, hurricanes, and earthquakes. In September 1978

the Federal Emergency Management Agency was established to consoldiate all emergency preparedness and response activities.

GAO AUDIT REPORTS: January 1977 - December 1978

Operation of the National Flood Insurance Program and disaster relief programs in Johnstown, Pennsylvania flood, (CED-78-114, 5/5/78)

Operation of Farmers Home Administration's Disaster and Emergency Livestock Credit Programs, (CED-78-136, 8/18/78)

16. Encouraging and fostering economic development in communities through improved public facilities

Work in this area deals primarily with Federal efforts to improve the quality of rural life, the delivery of public works assistance, and the provision of public facilities such as water and waste disposal systems necessary to accommodate and support economic growth. Past work was directed at two objectives:

--Improving the effectiveness of public works programs in developing the economies of communities, and

--improving the effectiveness of Federal community facility programs to assist developing rural areas.

GAO AUDIT REPORTS: January 1977 - January 1979

Observations concerning the Local Public Works Program (CED-77-48, 2/23/77)

Changes proposed for the funding of public works projects would expedite economic development and job opportunities, (CED-77-86, 7/7/77)

Selection process used for final round of Local Public Works Program - adequate but some problems experienced, (CED-78-36, 3/20/78)

Loan management procedures by HUD and EDA on Rend Lake Conservation district water project, (CED-78-89, 4/6/78)

Construction starts under the Local Public Works Program, (CED-78-140, 8/4/78)

Farmers Home Administration's use of grant funds for water and waste disposal systems, (CED-77-109, 8/17/77)

Improvements needed in the administration of Farmers Home Administration's Water and Waste Disposal Program, (CED-77-116, 9/1/77).

Management of Farmers Home Administration's Water and Waste Disposal Program Needs to be Strengthened, (CED-78-61, 3/13/78)

Minority firms on local public works projects--mixed results, (CED-79-9, 1/16/79)

17. Federal efforts to achieve balanced national and regional growth

Government at all levels has been basically passive in the migrational flow of people, in the concentration of industrial development, and in the forging of growth policies. Local government activity has been marked by economic competition, exclusionary zoning, and building code anarchy. State governments usually have been indifferent to growth changes and rarely willing to challenge the local government status quo. The Federal role has been wholly contradictory. On one hand, Congress enacts areawide planning requirements and strengthens regional bodies. On the other hand, the Federal-State highway program, FHA's activities and location decision of Federal agencies have collided head on with long term urban development needs. The result of all this has been to accentuate wrongway migrational patterns of people and business; to forge a white, middle-and-high-income noose around the increasingly black and poor inner city; and to subject much of rural America to a continuing course of gradual erosion.

18. Capacity of rural communities to deal with housing and community development programs

Rural population was declining slowly from 1940 to 1970, but since then there has been an increased tendency for families to settle in rural areas. Rural areas are now growing at a rate double the total U.S. population growth rate. Federal aid to State and local governments approached $60 billion in fiscal year 1976--about one-fourth of total State and local spending. Assignments in this area would deal with the capacity of rural communities to obtain and administer funds from the numerous Federal housing and community development programs.

19. Evaluation of Federal efforts to minimize adverse effects on communities from civil disorder

This area involves the efforts of the Federal Insurance Administration in administering programs that (1) enable businessmen and residents of homes and apartments to purchase burglary and robbery insurance in States where there is a critical problem of crime insurance availability at affordable rates which is not being resolved by appropriate State action, and (2) assure availability of essential insurance coverage for urban property, particularly that located in areas possibly subject to riots or civil disturbance, by providing reinsurance to insurers against catastrophic losses from riot or civil disorder.

GAO AUDIT REPORTS: January 1977 - December 1978

Operation of the fair access to insurance requirements plan, (CED-78-121, 5/31/78)

CHAPTER 3

ISSUES MERITING PRIORITY ATTENTION

HOUSING RELATED:

EVALUATION OF THE NATION'S EFFORTS TO HOUSE LOWER INCOME FAMILIES

The Housing Act of 1949 set a national goal of "a decent home and suitable living environment for every American family." The attainment of that goal has been elusive even though many Government-subsidized housing programs for lower income families 1/ have been established since 1937.

Many Americans do not have the financial means to obtain suitable housing. HUD estimated recently that there were 18 million families in this country needing some form of housing assistance. Six million of these families are presently living in housing considered to be substandard, ten million are spending a disproportionate share of their incomes for housing, and the remaining two million are living in over-crowded housing.

Federally-sponsored housing programs of the past have generally been production oriented and an attempt to increase the supply of housing. Under these programs, rental and home-ownership units were produced which accommodated varied lifestyles and needs of lower-income families. Rural areas were accorded a share of the new dwellings and both profit and nonprofit developers were allowed to participate.

Early in the 1970s, concern about the subsidized housing programs began to emerge. Homes in certain parts of the country were being abandoned; overproduction of homes was apparent elsewhere. The cost of construction of units under certain of the programs came under attack. In addition, the programs were criticized from the standpoint that they intensified the problems they were intended to solve by concentrating the poor in housing projects and burdening them with the stigma of being wards of the Government.

1/Generally refers to families with incomes of less than 80 percent of an area's median income.

In response to these problems, many of the federally assisted housing programs were suspended by the Nixon Administration in January 1973. Since then, there has been some shift in emphasis from production oriented programs to programs that make recipients a part of the general market by providing them funds or the means to compete for existing housing in neighborhoods of their choice. Two such programs are the section 8 leased-housing program authorized by the Housing and Community Development Act of 1974 and the experimental housing allowance program which got underway in 1973. These programs benefit primarily urban areas. To improve the quality of life in rural America, the Farmers Home Administration's section 502 program makes available direct loans with reduced interest rates to lower income families seeking suitable housing. This program is a large one under which almost 122,000 loans were made and $2.5 billion was obligated during fiscal year 1977.

Some controversy has existed concerning the extent to which each of HUD's subsidized housing programs should be used to meet the Federal commitment of assisting lower income families in obtaining housing. There are those who favor using the leased-housing and housing allowance programs almost exclusively. Others favor continued use of the older construction oriented assistance programs as well as section 8 leased housing. Another problem which is emerging is the high cost of providing housing assistance to the poor. Under the section 8 program, for example, fair market rents and the corresponding housing subsidies have risen since program inception to the point where estimated subsidy payments in fiscal year 1979 are expected to average from $2,200 to $2,750 for existing units and as much as $4,500 for newly constructed and substantially rehabilitated units.

Budget estimates for fiscal year 1979 show $1.3 billion as being needed to support HUD's assisted housing programs. This level of spending will support the reservation of 400,000 units; 344,000 section 8 units, 50,000 public housing units, and 6,000 units to be built on Indian reservations. Emphasis during the year will be on housing production (new and rehabilitated units), according to a top HUD official.

Our most recently completed work has included major reviews of HUD's section 236 program, its revised section 235 homeownership program, the dispersion of units and tenant characteristics under the section 8 and public housing programs, and the Federal Government's efforts to provide housing to Indians.

Our future audit efforts will center around the following objectives:

--Improving the Federal capacity to identify housing need and program its limited resources,

--improving Federal efforts to satisfy the Nation's subsidized housing needs, and

--insuring that housing produced provides the greatest benefit at the least cost.

Current assignments:

Review of rural housing, (CED, 38212)

Survey of Federal housing for low income elderly, and handicapped people, (CED, 38218)

GAO AUDIT REPORTS: January 1977 - January 1979

Major changes are needed in the new leased housing program (section 8), (CED-77-19, 1/28/77)

Review of HUD's Basic Homes Program, (CED-77-52, 4/11/77)

Poor design reviews and construction inspections of apartment project in Rhode Island, (CED-77-66, 6/3/77)

Review of HUD's decomentation to support fair market rents in Lancaster County, Pennsylvania, (CED-77-84, 6/16/77)

Need for fairer treatment of homeowner's claims for defects in existing insured homes, (CED-77-97, 7/27/77)

HUD's implementation of the revised section 235 home-ownership program for lower income families, (CED-78-16, 11/23/77)

Section 236 rental housing--an evaluation with lessons for the future, (PAD-78-13, 1/10/78 and PAD-78-62, 4/20/78)

Construction problems in a HUD-sponsored multifamily housing project in Naugatuck, Connecticut, (CED-78-40, 1/31/78)

Report concerning construction problems at several HUD-insured housing projects, (CED-78-39, 2/14/78)

Substandard Indian housing increases despite Federal efforts--a change is needed, (CED-78-63, 3/31/78)

HUD's cancellation of its allocation of section 8 elderly housing units in Harrisburg, Pennsylvania, (CED-78-150, 7/17/78)

Deconcentration of persons in the section 8 leased housing program, (CED-78-181, 10/20/78)

HUD's processing of a section 8 project in Milford, Ohio, (CED-79-7, 1/10/79)

Cost of section 8 housing could increase if owners sell or convert projects early, (PAD-79-43, 1/16/79)

MINIMIZING SUBSIDIZED HOUSING OPERATING COSTS AND IMPROVING ITS MANAGEMENT

Our Nation is faced with an increasing number of lower income families needing housing assistance. Therefore, federally-assisted housing, once produced, must be managed and maintained in a manner which enables it to continue providing lower income families the type of housing intended. This is not an easy job. Housing officials across the country have long struggled with the problem of deteriorating "public" housing--deterioration that was caused by rising expenses, inadequate funds for improvements, tenants' social problems, and poor management by local housing agencies and project owners alike. Problems such as these have many times caused the failure of housing projects and their corresponding removal from the lower income housing inventory.

The job of managing and maintaining assisted housing is not a small task. HUD, alone, is supporting about 3 million housing units at an annual expenditure of $4 billion and a total future runout cost considerably in excess of $100 billion over the lives of the mortgages and annual contributions contracts. This housing has been produced under numerous programs dating back to the early 1930s.

The high costs of supporting assisted housing today is reflective, in part, of the high rates of inflation experienced by the country in recent years. In many instances the rising operating costs of a housing project have far outstripped rises in tenants' incomes and their corresponding ability to meet the increased cost. Resulting from this has been a proliferation of types and amounts of supplementary

operating subsidies provided to public housing agencies and project owners to keep projects financially viable.

Each federally assisted lower income housing unit or project was constructed or otherwise made available for the purpose of providing housing for those who do not have the means to obtain such housing on their own. It is important that HUD and other Federal agencies with similar housing responsibilities find ways to ensure that such housing

--is maintained in a decent, safe, and sanitary manner;

--possesses desirable quality of life attributes;

--is managed economically and efficiently; and

--serves those for whom it was intended.

Our future work will be concerned with minimizing costs to operate and maintain subsidized housing and will be directed at the following objectives:

--How can improved management and cost-saving measures reduce cost to operate subsidized housing?

--Should federally provided operating subsidies be revamped?

--Is subsidized housing being maintained to insure its integrity and livability?

Current assignments:

Review of the quality of housing provided under HUD's section 8 program for existing housing, (CED, 38303)

Review of PHA's implementation of new legislative provisions relating to tenant selection and rent collection, (CED, 38304)

Review of rising rents and subsidies under HUD's section 8 program, (CED, 38306)

GAO AUDIT REPORTS: January 1977 - December 1978

Use of Farmers Home Administration financed rental housing for commercial office space, (CED-77-43, 3/11/77)

District of Columbia's rent establishment policies and procedures need improvement, (GGD-78-50, 5/17/78)

EVALUATION OF FEDERAL EFFORTS TO ENCOURAGE THE PRODUCTION OF NON-SUBSIDIZED HOUSING

The escalating costs of housing and the lack of an adequate supply of mortgage credit at reasonable terms have created serious problems for home purchasers and builders. At the same time, the construction of private rental housing has slumped and the vacancy rate in rental housing is at its lowest level in many years.

In May 1978 the average sales price of new single-family homes reached $63,000 and existing houses $54,800. The sales price increase for new homes in 1978 is estimated to be about 10 percent. House prices have increased at a faster rate than median family income. For example, from 1965 to 1976 the median sales price of new homes increased 120 percent compared to median family income of about 77 percent. The decline in affordability was not only caused by the greater increases in home prices but also by the rapid escalation of homeownership costs. These costs represent payments on the mortgage principal and interest, insurance premiums, property taxes, utilities, and repairs and maintenance expenses. Overall, homeownership costs increased about 200 percent during the 1965 to 1976 period. The significant increases in homeownership costs have resulted in homeowners using about 47 percent of their tax adjusted monthly family income to pay these costs, up from 31 percent in 1965.

For many years the Congress has stressed that homeownership is vital to maintaining the Nation's economy and quality of life. The Joint Economic Committee reported that the Congress should enact policies designed to increase the rate of housing starts to levels that are consistent with a National goal of 2.3 million units annually. Top priority should be given to programs designed to make new and existing housing affordable to more families.

Presently, the mortgage insurance and loan guarantee programs of the Department of Housing and Urban Development (HUD) and Veterans Administration (VA), and the loan program of Farmers Home Administration (FmHA) are several of the Federal initiatives which can have a positive effect in making homeownership more readily available to Americans. In addition, the secondary mortgage market activities of the Government National Mortgage Association, Federal Home Loan Bank Board, and the Federal Home Loan Mortgage Corporation are other Federal initiatives that are designed to facilitate the flow of capital into the housing sector.

To cope with the high cost of housing, HUD has implemented several innovative techniques to give increased impetus to the housing sector. HUD announced the graduated mortgage payment plan aimed at young home buyers seeking FHA insured mortgages. Under the plan, the mortgagor will have lower monthly payments in the early years, rising with the anticipated expansion of a family's income and leveling off in later years. To encourage apartment building, HUD increased the per unit limits on the mortgage amounts that it will insure under various programs. Also, HUD has embarked on an aggressive program for addressing some of the underlying reasons that have resulted in significant increases in the cost of housing as disclosed by its Task Force report in May 1968 and GAO's May 1978 report. Some of the areas to be explored are (1) major research to provide scientific data on aspects of housing construction and rehabilitation, (2) review of the impact of the national monetary and tax policies on the housing sector, and (3) ways to minimize impact of regulations that add significant costs to housing.

The Nation's rental housing supply has declined in recent years to where the vacancy rate--5 percent--is the lowest level in 30 years. The increasing demand for the available units has pushed rental rates up over 90 percent in the past 7 years. Rental units are in short supply because there is (1) an increased number of households, (2) fewer new rental units being constructed, and (3) an increase in the number of rental units being converted to condominiums.

Our future audit assignments will focus on improving Federal efforts to house more people through increased production, better access to credit and lower cost. Specific objectives are:

1. How can Federal efforts to promote home ownership be improved? Federal efforts to stimulate single family housing construction and affordability have resulted in additional housing starts, construction jobs, and increased mortgage funds. However, these efforts have been insufficient to enable many families to afford housing. The Federal efforts to provide alternative mortgage instruments has come under sharp criticism from many Congressmen as well as various consumer groups. They believe that the new instruments provide insufficient safeguards for the mortgagor and may be a means by which the lenders can perpetuate high interest rates.

2. How can the Federal Government encourage production of a sufficient number of multifamily rental units? Some housing experts have expressed concern that the Nation will face a serious shortage of rental units in the near future because of the low level of construction activity. It appears that HUD's emergency housing program for multifamily units and its program to refinance existing multi-family projects may not be sufficient steps to insure that adequate housing will be constructed in the future for many moderate income families.

3. What can the Federal Government do to minimize housing cost? In recent years, the cost of building, buying and operating housing has increased at a faster rate than family income. For many, the high cost of housing is not merely serious, but it is often an insurmountable crisis.

Current audit assignments:

Assessment of the Nation's dwindling rental housing supply, (CED, 38110)

Survey of FHA's role in todays housing market, (CED, 38811)

GAO AUDIT REPORTS: January 1977 - December 1978

Effectiveness of builder's warranties for new homes under HUD-insured and VA-guaranteed programs, (CED-77-20, 1/5/77)

Government National Mortgage Association's secondary mortgage market activities, (CED-77-28, 3/8/77)

Condominium homeownership opportunities could be increased, (CED-78-71, 3/21/78)

Why are new house prices so high, how are they influenced by government regulations, and can prices be reduced? (CED-78-101, 5/11/78)

What was the effect of the emergency housing program on single-family housing construction? (CED-78-155, 11/21/78)

EVALUATION OF FEDERAL EFFORTS TO MINIMIZE FORECLOSURES AND IMPROVE THE DISPOSITION OF ACQUIRED HOUSING

One of HUD's major objectives is to preserve the approximately 6,725 federally subsidized multifamily housing projects built for low and moderate-income families. HUD has identified 1,366 of these projects as being in three stages of distress:

--204 projects in HUD-owned acquired property inventory;

--950 projects undergoing foreclosure or with mortgages assigned to HUD; and

--212 projects in serious mortgage default.

An estimated 154,724 families live in the projects which were insured originally under sections 236 and 221(d)(3).

Because these programs were based upon a fixed subsidy which reduced the mortgage interest rate, the projects are particularly vulnerable to increasing maintenance, utility and other operating costs and taxes. Such costs can be defrayed only by rent increases. But, rent increases will often displace the very tenants these projects were designed to serve because tenant incomes have risen at a much slower pace than expenses. This inability to raise rents significantly has led not only to financial problems, but also to the physical deterioration of the projects. The past has shown that as troubled projects pass through the stages of default, assignment and ultimately, foreclosure, they deteriorate rapidly. By the time HUD actually owns them, most projects are often a blight to the neighborhood and require extensive repair. Troubled projects generally suffer from inadequate project income, inadequate HUD management, and inadequate on-site project management.

If present trends continue unchecked, HUD's inventory of troubled projects could rise to more than 3,000 projects (342,000 units) by 1982. This is the equivalent of roughly two years of government-assisted, multi-family new construction. HUD could easily become the owner of about 1,300 projects with an estimated 150,000 units. Losses to the insurance fund alone would be in excess of $3 billion. In some areas, HUD could own substantially all of the subsidized projects.

The families living in these projects are among the working poor, with median incomes about $5,500. If Federal subsidies were removed from these projects, most of the tenants would have to pay 30 to 40 percent of their income for rent. Any solution to help troubled projects which involves substantial increases in rent levels will clearly displace the majority of families now occupying these projects and defeat the original purpose of constructing the projects.

The projects are extremely valuable considering that the projects often are the only safe and sanitary housing available in their neighborhoods and the cost of building new housing is now twice the original cost of the troubled units.

A continuing problem faced by the Federal Government is the disposition of single-family housing it acquires through HUD, VA and FmHA programs. The acquired housing inventory amounts to about 44,000 units with HUD owning about 25,000 units. Also, there are about 5,000 units with mortgages assigned to either HUD or VA, many with delinquent mortgages. HUD holds about 500 mortgages which are over 3 years delinquent. HUD and VA will eventually acquire these units.

By virtue of ownership, the Federal agencies are charged with preserving and protecting the Government's interest in all property conveyed to it. In the past, the Federal agencies basic objective was to dispose of the property as promptly as possible while insuring a maximum dollar return on its investment. Recent changes to the basic policy have slowed the disposition rate, consequently, units are staying in the inventory longer resulting in larger losses when eventually sold. Serious damage is also occuring to many unoccupied units resulting in the units being temporarily lost as housing until the units are sold, renovated, and rented. This may take as long as 4 to 5 years.

Our past efforts have been related to improving Federal agencies underwriting practices and improving Federal efforts in acquiring, preserving, and disposing of housing projects. Future work will be focused on improving Federal efforts to maintain the viability of financially troubled federally insured and guaranteed housing by minimizing mortgage foreclosures and by getting acquired properties back into the housing market.

Current assignments:

Review of recent HUD policy changes on the management and disposition of HUD-owned multifamily housing projects, (CED, 38502)

Examination into rehabilitation activities for HUD-acquired multifamily projects, (CED, 38506)

Effectiveness of Federal efforts to foreclosure and sell single-family housing, (CED, 38507)

GAO AUDIT REPORTS: January 1977 - December 1978

HUD's appraisal and disposition practices for single-family properties, (CED-77-90, 6/23/77)

HUD unresponsive to multifamily real estate tax problems, (CED-77-125, 9/27/77)

Collection of credit reports fees by the Farmers Home Administration (CED-77-134, 10/7/77)

The Federal Housing Administration needs clearer criteria for underwriting single-family mortgage insurance, (CED-78-59, 3/13/78)

HUD needs to better assess financial soundness of multifamily residential projects before insuring them, (CED-78-70, 3/29/78)

ASSESSMENT OF THE DECISIONMAKING PROCESS FOR DEVELOPING HOUSING STRATEGIES

Housing laws today represent an accumulation of authorizations for some 46 unsubsidized and 20 subsidized programs. In managing these programs, there exist inconsistencies, duplications, lack of coordination, abuses, and inadequate monitoring of program activities.

From modest beginnings 40 years ago, the presence and influence of the Federal Government has grown dramatically. Numerous Federal housing and housing-related programs have been added to the statute books. The direct and indirect costs to the Federal Government to manage and operate these programs has grown to the point where the costs involved cannot be readily determined.

With the broad range of economic problems our Nation now faces, such as the growing and serious problems of inflation and substantial cost increases in goods and services, it becomes increasingly clear that the Federal Government must take drastic measures to eliminate nonessential spending in the production and management of our Nation's housing program.

The growth of domestic housing programs has taken place in largely unplanned, piecemeal fashion. This has resulted in too many overlapping programs, lack of coordination, and inequities. Various congressional reports have stated that some of the less needy now receive a disproportionate share of Federal housing benefits, while some who are more needy receive less.

Housing programs are plagued by inefficient management and charges that the cost to the Federal Government for many programs is more than what it would cost the private sector to produce and provide similar housing services. To function efficiently, housing programs must bring together private builders, private lenders, private housing sponsors, public agencies, and private purchasers. The number and complexity of programs at times acts as a deterrent to effective participation by these groups and hinders effective management of individual programs.

The Congress has declared many housing policies. Some of the more important of these housing policies are listed below.

--There should be housing production and related community development sufficient to remedy the serious housing shortage, the elimination of substandard and other inadequate housing through the clearance of slums and blighted areas.

--There should be as soon as feasible the realization of the goal of a decent home and suitable living environment for every American family.

--Housing production is necessary to enable the housing industry to make its full contribution toward an economy of maximum employment production and purchasing power.

Housing programs and policies have evolved over the years to a point where they are being used as a strategy to meet other national interests such as supplementing welfare programs and stabilizing the economy in periods of economic recession. A wide range of strategies can be used in meeting these goals such as direct subsidies, loans, insurance, tax policies or liberalizing credit terms. Priorities can be placed on types of units such as single-family, multifamily, condominiums, or segments of society such as middle income, lower income, veterans, the elderly, Indians, or rural families.

Existing housing programs throughout Government attempt to meet the housing and community development policy goals. When a crisis occurs, or when conditions change, choices have to be made regarding priorities. A sound policy framework could guide the decisionmaking. Present policies have no such framework, nor do they subscribe to an integrated set of goals.

To assess the decisionmaking process in the housing area, three questions should be addressed during the coming years:

1. How effectively do the strategies for existing housing programs mesh, overlap, and complement each other in meeting national goals?

2. How can the governmental framework for housing policy decisionmaking be improved to address the problems of today and the future?

3. Is the current data base and data collection system adequate to provide the information necessary for planning and implementing policy?

Past GAO reviews have focused on HUD's experimental housing allowance program. The experimental program has been testing the concept of housing allowances by providing direct cash assistance to eligible lower income households for their rental or homeownership payments. Past housing programs have not gone through such a research and testing phase.

Our future work objectives are to evaluate current housing strategies and goals and to identify alternative housing strategies and goals that can be realistically achieved in today's environment.

Current assignments:

Evaluation of the decisionmaking process used to develop the troubled projects strategy, (CED, 38706)

GAO AUDIT REPORTS: January 1977 - December 1978

An assessment of HUD's experimental housing allowance program, (CED-78-29, 3/8/78)

COMMUNITY DEVELOPMENT RELATED:

ASSISTING URBAN COMMUNITIES TO PREVENT AND ELIMINATE BLIGHT AND DETERIORATION

In 1949 our Nation established a goal of providing a decent home and suitable living environment for every citizen. Almost 30 years after setting this goal, an increasing number of our citizens live in blighted and deteriorated neighborhoods and communities.

Viable neighborhoods and communities are necessary for national stability and for the well being of the citizens who inhabit them. Today, the complex social and physical problems facing many of our communities threaten their viability. Many factors have combined to place heavy strains on the ability of existing public and private institutions to assure safe and wholesome living environments for all Americans.

Over the years, HUD and its predecessor agencies have administered numerous programs to stem physical deterioration of the cities and to renew those urban areas which have deteriorated beyond the point of reasonable salvagability. Recognizing past inadequacies in the Federal community development programs, the Congress in 1974 consolidated several existing categorical programs for community development into a single program of community development block grants (CDBGs). The primary objective of the new law is the development of viable urban communities by providing decent housing and a suitable living environment and expanding economic opportunities, principally for persons of low and moderate income. This objective is to be achieved through elimination of slums and blight and detrimental living conditions, conservation and expansion of housing stock, increased community services, improved use of land, spatial deconcentration of housing opportunities, and preservation of property with special value for historic architectural, or aesthetic reasons.

The Congress has authorized a total of $8.4 billion for this program through fiscal year 1977. The Congress has authorized a total of $12 billion for the program for the subsequent 3 fiscal years. For the first program year (1975) HUD awarded 3,153 grants for about $2.6 billion and in the second program year (1976) it awarded 3,358 grants for about $2.8 billion. During 1977 HUD awarded 3,402 grants for about $3.2 billion. For fiscal year 1978 HUD has been appropriated $4 billion for the block grant program.

GAO has made several reviews dealing with the block grant program including HUD's application and review requirements, the formula for allocating grant funds, communities efforts to meet environmental requirements, techniques used by HUD to evaluate communities' performance, and the administration of non-metropolitan discretionary block grants. In addition, GAO has made reviews of disposition of abandoned housing in major U.S. cities and adequacy of rehabilitation work under HUD's section 312 program.

Our future work objective is to improve governments' efforts to preserve and renew urban neighborhoods. Our work will be directed to: How effective are neighborhood preservation and renewal efforts? How can local government's capacity to eliminate blight and deterioration be improved?

Current assignments:

Review of urban renewal activities in San Antonio, Texas, (CED, 38466)

Survey of federally assisted rehabilitation efforts under the block grant and section 312 programs, (CED, 38468)

Review of urban homesteading programs, (CED, 38469)

Survey of the adequacy of construction work performed and local agency administration of section 312 rehabilitation program, (CED, 38471)

GAO AUDIT REPORTS: January 1977 - December 1978

Environmental reviews done by communities: Are they needed? Are they adequate? (CED-77-123, 9/1/77)

Effectiveness of the implementation of the block grant program, (CED-78-30, 1/24/78)

The District of Columbia needs a program to identify vacant houses and get them back on the market, (GGD-78-35, 2/22/78)

Housing Abandonment: a national problem needing new approaches, (CED-78-126, 8/10/78)

Management and evaluation of the community development block grant program need to be strengthened, (CED-78-160, 8/30/78)

The community development block grant program: discretionary grant funds not always given to the most promising small city programs, (CED-78-157, 8/31/78)

Review of the District of Columbia's application for block grant funds to establish a National Children's Museum, (CED-79-20, 12/5/78)

ASSISTING COMMUNITY DEVELOPMENT THROUGH LOANS AND GRANTS TO BUSINESSES

The economic and social health of the Nation's communities depends largely on the vitality of their tax paying, employment providing businesses. But many people interested in establishing or expanding businesses are handicapped by inadequate credit and management know-how, and find it difficult to compete with foreign businesses or the domestic corporate giants. Minorities and others who suffer from social or economic disadvantages find it particularly difficult to create and maintain viable businesses. The American farmer--the provider of products vital to continuing economic health on both the domestic and international scene--has an acute need for financial assistance to supplement credit available from private lenders. To help businesses overcome these problems several Federal agencies operate programs designed to give financial, procurement, marketing, and management assistance to business.

The Federal Government has identified certain segments of the business sector for special assistance including small businesses, minority-owned businesses, businesses located in rural or depressed areas, and businesses facing intense foreign competition.

The Small Business Administration (SBA) estimates that there are about 13.2 million small businesses in the country. Each year numerous small businesses fail due to inadequate financing and poor management. SBA recently found that small businesses have the same kinds of problems as larger businesses but suffer from them to a greater extent and concluded that "by almost every measure, small firms fare worse under changing economic conditions than do large businesses." Each business failure adversely affects the community.

Small businesses have extreme difficulty obtaining financing at reasonable rates because of the high risk associated with new businesses. Repeated surveys show that lenders and investors place a great emphasis on a firm being well established and having a proven earnings record extend-

ing over several years. Most small businesses cannot meet these requirements, therefore, no financing is available. Problems facing small business appear to have increased rather than diminished during the past years. Based on these trends, SBA projects that life will get harder rather than easier for the small businessman during the next decade.

Good management is critical to the success of a business as indicated by estimates that 9 of 10 business failure are attributable to management deficiencies. Small business owners often lack the education and resources necessary for a viable business. Also due to the characteristic combination of ownership and personal control found in small businesses, the owner/manager's energy, time, and attention are often thinly spread.

The problems of minority businesses are generally even more severe than for small businesses. A lack of a business tradition, language barriers, and racial discrimination are factors that limit opportunities for minority business ownership. According to the Office of Minority Business Enterprise (OMBE), in 1972 racial or ethnic minorities constituted 19 percent of the United States population but owned only 4 percent of the Nation's businesses and accounted for less than 1 percent of the United States gross business receipts.

The seriousness of the problems confronting minority-owned businesses is indicated by the results of two SBA programs designed to assist them. The 8(a) procurement program provides Federal contracts on a non-competitive basis to minority businesses enrolled in the program. The program is designed to "graduate" firms when they are able to compete without Federal assistance. Over the 10 year history of this program only 139 firms have graduated. The Economic Opportunity Loan Program provides loans to firms owned by low-income persons or firms located in areas of high unemployment or low-income. Most of these loans are made to minority-owned businesses. As of September 30, 1977, 12,857 of these loans had been repaid but about 18,000 had been charged off as uncollectable or were being liquidated.

In fiscal year 1977, minority businesses received loans (direct and guaranteed) and bonds valued at $531 million and Federal contracts totaling $1.2 billion. Recently, the President has announced his intention to triple the amount of Federal contracts awarded to minority businesses.

Economic conditions in rural areas are often not conducive to business growth due to inadequate financing and

public services such as transportation and health services. About 14 percent of rural families live in poverty compared with 11 percent in urban areas. Also, about 43 percent of the Nation's substandard housing is in rural areas, though these areas account for only 32 percent of households. Recent legislation has committed the Nation to revitalize and develop rural areas as a means of achieving a balanced national growth. The development of businesses in rural areas would contribute to the solution of many of these problems.

Our Nation has grown and prospered economically over the past three decades, but this prosperity has not been evenly distributed among areas of the country. Many areas have remained economically stagnant. The Economic Development Administration (EDA) provides business development loans to encourage business and industry to build or expand in the depressed areas.

Over the years, legislation has been enacted to protect the domestic producer from foreign competition and also to promote more open and equal international trade. In passing the Trade Act of 1974, the Congress recognized that increased imports resulting from expanding international trade could adversely affect certain firms within the United States. Therefore, the Congress provided monetary assistance for those firms injured by imports. This assistance was designed to bring about an adjustment to changed economic conditions caused by international trade patterns. Section 280 of the act requires GAO to conduct a study of adjustment assistance programs and to report the results to the Congress no later than January 31, 1980.

Most of our past efforts have been the result of numerous congressional inquiries regarding SBA's 8(a) procurement program and 7(a) loan program and SBA's and FmHA's disaster loan programs. Self initiated reviews produced reports on progress and effectiveness of FmHA's business and industrial loan program; need for OMBE to do more in starting and maintaining minority businesses; need for SBA to obtain financial statements to properly assess the quality of its management assistance services; and the usefulness of the small business investment company program.

Future assignments will be directed to improving and maintaining the viability of businesses that contribute to community economic development. Assignments will focus on the following objectives: (1) determining whether Federal agencies have organized themselves so as to deliver business assistance and services in the most efficient and effective manner; (2) determining whether Federal agencies follow sound underwriting practices in administering business loan programs; (3) assessing whether the management support services of the business assistance agencies are contributing to good management and control of programs and activities; and (4) determining the effectiveness of Federal assistance to minority-owned businesses.

Current assignments:

Review of farm credit programs and coordination between lenders, (CED, 06914)

Review of the Farm Credit Administration's assistance to farmers, (CED, 06915)

Effectiveness of SBA's surety bond guarantee program, (CED, 07787)

Effectiveness of SBA's actions on GAO's recommendations made under P.L. 93-386, (CED, 07788)

Effectiveness of SBA's economic opportunity loan program, (CED, 07789)

Effectiveness of delivery systems used by Federal agencies to provide assistance to business, (CED, 07790)

Review of selected aspects of OMBE contract with BDC/ a one-stop service center, (CED, 06307)

Review of long-term implications of FmHA subsidized and guaranteed loan programs, (PAD, 97143)

GAO AUDIT REPORTS: January 1977 - December 1978

Information on the closure of SBA's Marshall, Texas District Office, (CED-77-22, 1/6/77)

Procedural operation of Farmers Home Administration in Wisconsin, (CED-77-29, 2/10/77)

Department of Defense program to help minority-run businesses not working well, (PSAD-77-76, 2/28/77)

Assistance to non-rubber shoe firms, (CED-77-51, 3/4/77)

Business development loan to one company was inadequately justified, (CED-77-111, 8/12/77)

FmHA's business and industrial loan program can be improved, (CED-77-126, 9/30/77)

The Office of Minority Business Enterprise could do more to start and maintain minority businesses, (CED-77-136, 11/10/77)

Ways to increase the number, type, and timeliness of 8(a) procurement contracts, (CED-78-48, 2/1/78)

Information on selected activities of the Office of Minority Business Enterprise, (CED-78-51, 2/16/78)

The Small Business Investment Company Program: Who does it benefit? Is continued Federal participation warranted? (CED-78-45, 3/3/78)

Uncertain effectiveness of the SBA's management assistance program, (CED-78-64, 3/15/78)

An analysis of how eligibility criteria are applied for participation in the 8(a) program, (CED-78-92, 3/31/78)

Should lenders assume more responsibility in the SBA 7(a) loan program?, (CED-78-88, 4/4/78)

Need to improve servicing of direct loans in EDA's business developing assistance program, (FGMSD-78-34, 5/15/78)

Difficulties in coordinating farm assistance programs operated by FmHA and SBA, (CED-78-118, 5/25/78)

What is a small business? The SBA needs to reexamine its answer, (CED-78-149, 8/9/78)

ASSESSMENT OF EFFORTS TO ASSIST ECONOMICALLY DISTRESSED COMMUNITIES

Recent studies have shown that half of the Nation's cities with populations greater than 500,000 and one-fourth of the cities over 50,000 are now in distress. About 250 cities both large and small are considered to be distressed. In some cities social and economic difficulties, environmental pollution, and neighborhood and housing decay often strike at once, paralyzing a city's ability to make ends meet and respond to the legitimate needs of residents. Attempts to solve one problem often make the others worse. The result is a city in distress. Cities and communities most in distress are those where population decline and high levels of unemployment and poverty occur together.

Numerous older cities face escalating costs because of inflation, the need to provide services to large numbers of often unemployed poor people, and the need to maintain aging facilities. Unfortunately, many cannot meet the increased financial burdens. Much of their taxable wealth (in the form of more affluent residents, business and industry) is moving away and their overall economies are not stable. They find it difficult to provide a decent environment, decent jobs, and decent neighborhoods to large numbers of their residents. They are unable to protect billions of dollars invested in roads, housing, transit, sewer and water systems.

The Carter Administration announced in March 1978 the first National Urban Policy to ever address comprehensively the problems and promise of America's cities and neighborhoods. The National Urban Policy will require a major overhaul of most Federal programs aimed at cities, a process which has already begun, and the establishment of new programs. For example, it is expected that over 160 changes in 38 existing Federal programs will take place to target funds more to urban needs. In addition, 30 components of the proposed Urban Policy will require new legislation.

Currently through the 38 existing programs about $6 billion a year is directed in aid to States and cities. The new policy calls for new spending or tax changes that, if enacted by Congress, would cost $2.4 billion in fiscal year 1979, and $4.6 billion in fiscal year 1980. The bulk of the new funds would be used to stimulate employment and business investment in urban areas by using Federal loan guarantees, employment tax credits, subsidized interest rates and direct public-works spending.

Our future work will be directed toward three objectives:

--Improving the planning and coordination of Federal efforts to assist economically distressed communities,

--Improving the implementation of Federal economic development programs and initiatives, and

--Encouraging the private sector to assist economically distressed communities.

GAO AUDIT REPORTS: January 1977 - December 1978

None

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- Subcommittee on Rural Development

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- Subcommittee on HUD-Independent Agencies
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Select Committee on Indian Affairs

Select Committee on Small Business

Joint Economic Committee

Joint Committee on Taxation

House of Representatives

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