

HUD Issues Property Disposition Memo Affecting “Section 311”

On May 31, HUD’s Office of Multifamily Housing Programs issued a formal Memorandum providing instructions regarding property disposition requirements for FY 06. This memo is not on HUD’s web site and its existence was not made public; however, a copy was obtained by local housing groups and shared with preservation advocates around the nation through the National Alliance of HUD Tenants (NAHT). A copy of the memo is available at www.nlihc.org/regwatch/tp1.pdf.

A major feature of the memo concerns implementation of “Section 311” of the FY 06 Appropriations Act. Also known as “the Schumer Amendment” after Sen. Charles Schumer (D-NY), Section 311 requires HUD to keep project-based Section 8 contracts at buildings when it sells HUD-owned properties (acquired through foreclosure or deed-in-lieu) or sells properties at foreclosure (because the owner defaulted on a HUD-insured mortgage).

Section 311 Background

Section 311 addresses the problem of HUD eliminating project-based Section 8 subsidies when selling a property at foreclosure or when HUD obtains a project through foreclosure and subsequently sells it to a new owner. Section 311 requires HUD to keep project-based Section 8 units at a foreclosed property it transfers to other owners, rather than switch to a tenant-based Housing Choice Voucher. Keeping the project-based Section 8 with the property (rather than “vouchering out”) makes it easier for the new owner to obtain financing and therefore sustains the stock of affordable housing. If it is not economically feasible to keep project-based Section 8 units at the HUD-held property, HUD may, in consultation with tenants, transfer the project-based Section 8 to another property and thereby preserve the subsidy. (HUD could also substitute other assistance, presumably tenant-based vouchers.)

The text of Section 311 of the FY 06 Appropriations Act is at the end of this paper.

Problems in the May 31 Memo

There are a number of problems with the policies presented in the memo.

A. Feasibility Analysis (page 6)

When making its way through the Conference Committee, House negotiators created a major loophole in Section 311. HUD can determine that it is not feasible to continue project-based Section 8 at a property based on cost or on “other factors.”

The May 31 Memo requires HUD to conduct a Feasibility Analysis using four major criteria, any one of which HUD can use to determine that it is not feasible to continue project-based Section 8 once a property is sold.

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A. Feasibility Analysis (page 6), *continued*

1. Cost to Rehabilitate the Property (page 6): Continuation of a project-based Section 8 contract after a property is sold might be determined by HUD to be infeasible if – the pre-foreclosure Section 8 rents are not sufficient to cover both operating costs and repayment of loans inevitably needed to bring a property up to standard after neglect by the prior owner.

This criterion is likely to lead to a determination of “infeasible” because the memo (page 5) limits rents to pre-foreclosure sale rents, adjusted only once a year using the very modest “operating cost adjustment factor” (OCAF).

Advocates think the feasibility standard should consider all available resources, including future rent increases under a renewed Section 8 contract as permitted by HUD’s Mark Up to Market programs.

2. Environmental Conditions (page 6): Continuation of a project-based Section 8 contract after a property is sold might be determined by HUD to be infeasible if – there are environmental factors that either HUD or the purchaser cannot mitigate without spending too much money. Factors mentioned in the memo include noise, air pollution, flooding, site stability, soil erosion, and hazardous industrial operations.

Relative levels of noise and air pollution might be factors easily exploited to avoid continuation of a project-based Section 8 contract.

3. Neighborhood Conditions (page 7): Continuation of a project-based Section 8 contract after a property is sold might be determined by HUD to be infeasible if – conditions in the neighborhood have significantly deteriorated due to inadequate police or fire protection, high crime rates, drugs, or lack of public community services.

A critical component essential for improving neighborhoods is stable, attractive, affordable housing.

4. Contradictory Local Plans (page 7): Continuation of a project-based Section 8 contract after a property is sold might be determined by HUD to be infeasible if – local plans such as land use plans or ConPlans do not call for multifamily housing in the area.

B. Right of First Refusal (page 10)

The law requires HUD to notify units of local government (ULGs) that it intends to foreclose on a HUD-held mortgage and to give the ULG an exclusive option to make an offer within 30 days to buy it (the Right of First Refusal) if HUD acquires title as high bidder at the foreclosure sale.

The May 31 memo introduces three problems:

- HUD requires the ULG to waive all delinquent municipal liens on the property such as back taxes and unpaid utility bills.
 - *This could discourage a ULG from making an offer to buy.*
- HUD will determine the sale price of the property based on the value of market-rate rents and HUD's estimate of operating expenses.
 - *HUD should attempt to take title of a property by bidding the amount of the outstanding mortgage at auction. If HUD acquires title to the property, it has more flexibility to make emergency repairs or to plan for an appropriate sale to a preservation purchaser.*
- The market value will not reflect any costs of needed repairs or costs due to affordable use restrictions.
 - *The price of a building should reflect its condition; many will need major repair due to the neglect of the foreclosed owner.*

C. Section 8 Payments Will Not Begin Until All Units Meet HQS (page 5)

The purchaser must ensure that any unit under the project-based Section 8 contract meets HUD's Uniform Physical Inspection Standards before Section 8 project-based assistance is made available. Unit inspections will not take place more frequently than once a month.

- *Because many foreclosed properties are likely to need major rehab, HUD should allow transitional Section 8 payments so that the new owners can make the repairs.*

D. Resident Consultation (page7)

Section 311 requires HUD to consult with residents if the project-based Section 8 contract will not be maintained when a property is sold. The May 31 memo says residents will not be notified that the project-based Section 8 contract for their building will be terminated until the end of the road – after the feasibility analysis is completed and two layers of HUD have agreed on termination. Residents will be given 30 days to respond to and comment on the foreclosure notice.

- *Residents should be notified as soon as there is a proposed decision to proceed with foreclosure.*

E. Tenant Protection Vouchers (page 8)

If HUD decides to sell a property without a project-based Section 8 contract, Tenant Protection vouchers will be requested for all eligible current residents. However, HUD will only provide Tenant Protection vouchers for units under lease, not for any vacant units.

- *This will result in diminished rental assistance for the community as a whole.*

Text of Section 311 of the FY 06 Appropriations Act

Notwithstanding any other provision of law, in fiscal year 2006, in managing and disposing of any multifamily property that is owned or held by the Secretary of Housing and Urban Development, the Secretary shall maintain any rental assistance payments under section 8 of the United States Housing Act of 1937 that are attached to any dwelling units in the property. To the extent the Secretary determines that such multifamily property owned or held by the Secretary is not feasible for continued rental assistance payments under such section 8, based on consideration of the costs of maintaining such payments for that property or other factors, the Secretary may, in consultation with the tenants of that property, contract for project-based rental assistance payments with an owner or owners of other existing housing properties, or provide other rental assistance.

Thanks to the National Housing Law Project, New York State Tenants & Neighbors, Community Services Society of New York, and Urban Homesteading Assistance Board for an initial assessment of the May 31 Memo.