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A CONSUMER ORIENTED PROGRAM
TO PROVIDE A DECENT HOME
FOR ALL AMERICAN FAMILIES
AT MINIMUM SUBSIDY COST

Statement by

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to the

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Committee on Banking and Currency
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A CONSUMER ORIENTED PROGRAM
TO PROVIDE A DECENT HOME
FOR ALL AMERICAN FAMILIES
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I want to express my appreciation to you, Mr. Chairman, and to the other members of your distinguished Subcommittee, for the opportunity to express my views and make recommendations, on HR 9688, the Housing and Urban Development Act of 1971.

Before beginning my testimony, I should like to note that I am appearing as an individual with a long-time interest in and connection with the nation's housing programs, and not in my capacity as a member of the Federal Reserve Board.

Let me begin by congratulating the Subcommittee on Housing of the House Banking and Currency Committee, Mr. Chairman, upon adopting-- in the proposed Housing and Urban Development Act of 1971--an invigorating new view of our housing problems, and realistic solutions to them. I would note that HR 9688 rests upon the excellent and open-minded work of three preparatory panels, headed by Representatives Sullivan, Ashley, and Moorhead, that developed, with the help of a wide range of consultants, a series of studies that comprise, in my view, a most valuable analysis of the nation's housing situation and possible approaches to our housing problems.

I think HR 9688 strikes the essential note when it includes, in its preamble, the following goals among its chief purposes:

"To broaden the national housing goals . . . with emphasis upon the preservation and more efficient use of the existing housing stock and upon the revitalization of declining neighborhoods . . ."

In placing substantial emphasis upon making use of the full stock of serviceable housing, HR 9688 raises the fundamental possibility of shifting governmental assistance from the building of new housing to the housing of people. That, in my view, is where the aim should be, and I consequently regard HR 9688 as a potential legislative watershed in efforts to provide every American family with decent housing.

While I stress the need for reshaping parts of HR 9688, I would emphasize that the bill you are considering is replete with timely proposals for redirecting our housing activities, and the addition of new efforts that are both desirable and needed. Since I have no quarrel with the general direction of this legislation, I will not use my time today

to review HR 9688 and comment on it in detail. Instead, I want to offer you an institutional addition to your proposals that, in my opinion, is essential if HR 9688 is to carry out its purposes.

At the same time, I want to suggest an alternative method of handling current home ownership subsidies under the 235 and related programs. I think this approach would result in substantially lower total subsidy costs, and would permit the Government to share in capital gains that its financial support of housing programs makes possible.

I would like, first however, to state briefly a set of concepts that I believe must underlie a housing program that will do what a housing program should do, chiefly: serve the needs of people, and help create communities that lift the quality of our lives.

A Set of Underlying
Concepts for a Consumer
Oriented Housing Program

I consider the following general concepts to be basic to consumer oriented Federal legislation for a realistic, effective, low cost program to provide decent housing, and a good neighborhood, to every American family:

First -- A housing--not a construction--program. As I have already indicated, the program should be a program for putting people in good housing and helping them to stay there, not a program essentially limited to the production and financing of new housing.

It should, consequently, provide assistance for using the whole range of housing, from the rehabilitation, preservation, maintenance, and financing of existing units that low and medium income families can afford to buy, to the production and financing of new housing for these and other families. I will return to this fundamental point later in my testimony, as I will to some of the other basic concepts I am only touching upon here.

Second -- Reduction of both governmental involvement and outlay. The program should aim at substantially reducing the involvement of government, and the cost to government.

It seems implicit in much of the analysis produced, Mr. Chairman, by the Subcommittee's panel studies, that the current effect of government's role in housing is to narrow, rather than to expand, the ability of government to meet many of our housing problems. For instance, in terms of making use of existing housing, current programs make it difficult, if not impossible, to utilize older structures in many neighborhoods.

Further, when aid is centered, as it is now, on the building of new housing projects, many government projects run into constraints in the shape of zoning, racial, economic and other local requirements that give practical effect to political resistance to the relocation of the poor in suitable housing.

Third -- Maximizing consumer choice. As governmental intervention is minimized, consumer choice should be maximized.

For example, your reports correctly stress the importance of locating housing in reasonable proximity to jobs. This is not only a matter of convenience to the family, although that is important. It also reduces daily traffic flows, relieving expensive traffic congestion and abating pollution. The building of sprawling housing developments at the far reaches of cities locates housing without regard to the location of jobs. Individual families, making their own decisions and making use of the existing housing stock, can come much closer to satisfying their own needs and desires than can any outside agency.

The way to give each family the widest range of choice in housing is to make the whole stock of housing subject to governmental assistance. Under such conditions, consumers can meet their own needs without waste of their own or government funds.

Fourth -- Maximizing the use of free enterprise. The program should bring market forces to bear on those who produce, rehabilitate, and finance housing, to make available, for low and medium income families, housing that serves both human and urban requirements.

By contrast, many current programs operate in such a way that the Federal Government guarantees a rate of return to the producers and financiers of new lower income housing so long as the housing meets a list of physical criteria. There is little, if any, regard for the effect of the new housing developments upon communities, and insufficient thought for whether the housing built is in the right location, is the right size, provides a good neighborhood environment or meets the other human needs that it is the primary duty of housing to serve.

Fifth -- Counseling. Any realistic program must make available-- as HR 9688 does--advice to consumers on how to find, finance, repair, maintain, and make the best use of housing.

The choice of the right type, size, and location of housing, and deciding what is the right price to pay for it, are among the most difficult decisions--with the greatest penalty for being wrong--that most families ever make. Further, few consumers have valid experience to guide them in making these housing decisions.

Sixth -- Reduction of the cost of housing programs. Housing program costs can be reduced in three main ways: by avoiding unnecessary subsidies; by utilizing the homebuyer's "pride in home" to keep down the cost of repairs and maintenance; and by making available the entire stock of basically sound units for subsidy programs.

One of the concepts implicit in HR 9688 is avoidance of unnecessary subsidies for the production and financing of housing. The housing market is dynamic. We should avoid a system that freezes into existence subsidies for housing to those who do not need them. This may happen, in the production of new housing, as the size and income of families alter, as the market for housing changes, or because of the difficulty of fitting subsidies to actual needs.

In housing, as elsewhere, "a penny saved is a penny earned." Many pennies--and many hundreds of dollars per household--can be saved through the do-it-yourself efforts of homebuyers, motivated by pride in a home of their own--and of their own choice--to keep their property up, and even to improve its value.

Failure to make use of this "pride in home" factor results, on the contrary, in the decay of housing, and its subtraction from the available stock. We will all be better off if families are motivated to improve their homes, and the number of available units, in this way, is expanded at minimum cost to the economy and government budgets.

Seventh -- Overall goals. Finally, let me stress a concept that I believe is vital: the concept of consciously linking our housing programs to the achievement of other closely related national goals.

One such goal is the resuscitation of our cities--where property values in many neighborhoods with excellent but deteriorating housing are suffering badly. We need to build, or rebuild, neighborhoods that have a healthy variety of cultural, racial, and income elements, and an interdependent mixture of private homes and small commerce to serve locally the daily needs of the people of the neighborhood. Communities made up of such neighborhoods invigorate and enrich the lives of those who live in them, ease the achievement of educational and social goals, and renew our American sense of unity in plurality.

Our current approach to our housing needs frequently has done the opposite. The focus on the financing of new housing--and its concomitant neglect of the existing housing stock which shelters 97 per cent of our families in any one year--has fragmented our cities and segregated their inhabitants by income, some in rotting slums, and others in sterile suburbs. In both cases--in the cultural gutter of the slums and in the cultural wilderness of the suburbs--our children have grown up as urbanites who do not know what a city is. The lack of variety and

wholeness in their environment, and its lack of creditability as a community, have contributed to depriving a great number of our younger people of a sense of attachment to home or neighborhood, and have helped to alienate them from the nation's traditions and values.

Before I go on to describe an organizational vehicle for providing all American families with decent housing, let me make two points to avoid misunderstanding.

First: I am not suggesting any slowdown in new private dwelling construction. The number of new housing units built depends, basically, upon the growth of households and their ability to pay for a suitable level of housing, not upon the construction of housing for the poor. Our total needs for housing are so great that, if we maintain as our goal a good home in a good neighborhood for every American family, it will not be possible to slow down the building of new dwelling units. Many of the proposals in HR 9688 would have the effect of giving such building more relevance to the needs of people--especially the need of people to be located in reasonable proximity to their work--and to more rational urban development. This new housing will be occupied by people whose income permits them, without subsidy, to purchase new and larger homes or to rent new apartments, outfitted with the latest conveniences and comforts. It is only through this process of freeing existing housing that an adequate stock of sound homes for low and medium income families can become available.

In addition, if new housing can be built competitive with existing units, the program I am presenting will open it to subsidization. What we need to do is free the output of our entire housing industry to consumer choice. If we can solve the problem of protecting the consumer, we can avoid the current difficulties which arise from earmarking only a portion of our stock for use in the subsidy program. We should free the construction industry and local governments from dependence on pre-authorization of each unit by HUD.

In addition, families occupying new housing will still be receiving considerable governmental assistance, by making land and community facilities available, by spurring innovations in construction techniques, by providing mortgage funds at reasonable rates through the secondary market operations of FNMA, GNMA, and other governmental agencies, and through efforts by the monetary authorities to avoid concentration of the effects of monetary restraint upon the availability and cost of housing credit.

To a substantial degree, housing standards will be increased to the extent that we can arrest the deterioration of the existing stock. A substantial net saving in Federal housing subsidy outlays can be achieved by shifting subsidy support to the rehabilitation, repair, maintenance, and financing of existing housing for families with income levels that do not permit them to purchase most of the new housing now being built.

The demand upon our national resources and the Federal budget are so great that such savings in subsidies will not bring about a diminution in total construction. The repair and refurbishment necessary to keep older, but sound, housing livable will involve considerable construction outlays. More important, any savings can be used to assist in financing of existing shortfalls in our urban infrastructure.

The adoption of an effective program aimed at putting every American family into a decent home, in a neighborhood with good streets and sidewalks, adequate water and sewage installations, good lighting, reasonable amounts of parklands and other public recreational and community facilities, will, while increasing the standard of life for all, create, net, as much or more construction activity and employment than would be created by continuing to focus on public subsidies to the construction of new housing.

Second: Let me deal with another commonly expressed and somewhat contradictory fear: that an effort to put poor and medium income families into decent homes will be self-defeating because it would bid up the cost of existing housing. There are two key factors. The first, mentioned above, is that a continued high rate of new housing construction will permit families with upward mobility, provided by a generally rising income stream, to vacate something like 3 to 5 per cent of existing homes each year. Their moves in turn lead to others. A fifth of our housing stock becomes vacant every year. In addition, more of the new units will be available to consumers who can search out individual units that fit their needs and their pocket-books (augmented if necessary by a subsidy).

The second factor is that governmental financial support to locate low and medium income families in existing housing means an increase in the availability of funds for the repair and rehabilitation of basically sound housing and a reduction in the number of habitable units which are lost each year. A major problem in many communities at present--and one that would diminish if governmental help were available to make existing housing available to many who cannot afford it in the absence of such help--is the abandonment of a large number of housing units annually. The resulting increase in the supply of habitable units would tend to decrease any upward cost pressure.

An Organizational Vehicle for
Making Existing Housing Available
for Ownership by Low and Medium
Income Families

What is needed is a vehicle to implement some of the housing reforms proposed by HR 9688. This should be a consumer oriented, locally focused, one-stop housing agency, where the low income family can be offered a logical choice of buying or renting, and the homebuyer can be sponsored, financed, and advised on a coordinated basis. Such enterprises need to be organized wherever, in the cities and in rural areas, a need exists for large-scale assistance to those whose income does not enable them to obtain adequate housing. There might be many of these establishments overlapping geographically and varying in form.

The reason for such multiplicity--which would involve a great deal of variety in the details of their makeup and operations--lies in the importance of using insofar as possible the economies offered by competition and a free-choice mechanism. At the same time, these enterprises must be part of the community they serve, must command its respect, and must be fully familiar with its problems and outlook. They must be knowledgeable about and able to enlist the services of locally available skills of nearly every type, from carpentry to marriage counselors.

I am putting before you a proposal for such a type of enterprise designated as Home Ownership Promotion Enterprises (HOPEs). I have based the design of HOPEs upon my knowledge of the needs for housing and the successes and failures of numerous other organizational vehicles throughout the country. It is my suggestion, Mr. Chairman, that your Subcommittee recommend the addition to HR 9688 of such an institutional vehicle for accomplishing the housing reforms you are proposing. I want to suggest the general approach which a true housing program should take, an approach which builds on the implicit concepts mentioned earlier: minimum governmental intervention, maximum consumer choice, use of the existing market mechanism, "pride in ownership," and the avoidance of unneeded subsidies. I think the objectives of HR 9688 will be hard to reach without such an organizational vehicle.

I turn now to a description of the Home Ownership Promotion Enterprises as I envisage them.

There would be one or more HOPEs in each Standard Metropolitan Statistical Area (SMSA). Their fundamental task would be to assist low and medium income families to find and purchase, when possible, the house that suits them and that they need. For families for whom renting would be a better choice, they could serve to administer parts of a housing allowance program. They would conform to national, State and local housing policies. They would administer certain existing and proposed housing subsidy programs.

A HOPE would be formed by those with existing skills and interests in housing such as groups sponsored by financial institutions, municipalities, planning and housing councils, trade unions, churches, local housing cooperatives, the Foundation for Cooperative Housing, community groups, etc.

Each HOPE would be a non-profit, or limited dividend, or cooperative organization approved as a contractor by the Department of Housing and Urban Development. Recognition would be based upon a table of organization and plan of operation submitted to HUD by the HOPE. The prospectus submitted to HUD would identify the principals of the HOPE, and describe their qualifications. A HOPE would be staffed by high caliber professionals, assisted by volunteers drawn from community organizations.

A HOPE would be overseen by a board of directors drawn from a wide spectrum of civic groups and private firms with knowledge and experience in housing. Each HOPE would be expected to keep in friendly touch with responsible community organizations and to solicit the views of these organizations as to its goals and operations.

I attach a chart to show schematically some of the functions such organizations should include. Again, the specifics are not as important as the concepts and they would have to meet local conditions. Some of the functions that stand out are functions not now being performed under existing programs. Major among these required functions are:

- Impartial advice to the home seeker on whether to purchase or rent;
- Aid in selecting the proper house;
- Aid in judging values and financing;
- Counseling on occupancy and ownership problems;
- A non-governmental and non-FHA institutional alternative for obtaining HUD aid in financing and counseling.

The HOPE could contract with existing institutions for necessary services, such as financial services and counseling. The important features would be to make use of existing market skills and economies of scale while devising enterprises whose pay-off functions would be in terms of successful family housing experiences rather than sales or rental of units.

The HOPEs would also be able to contract with HUD to furnish housing allowance certificates to those families whose needs could be better met by renting than by buying a house.

The autonomous counseling service of the HOPEs would assist the family to choose housing adequate and logical for its needs. In helping a family choose the type of housing it needs, the counseling arm of the HOPEs should have available to it the service of those with expert local knowledge of existing housing opportunities and costs. The basic objective would be to help the would-be homebuyer avoid prejudicing his chances of being a successful home purchaser by making a bad bargain at the outset.

In the operative diagram, under the families who buy rather than rent, I have shown two alternative programs. One would be based on the assumption that with proper aid to the buyer, the FHA program for existing homes could be made to work and could be applied to the entire standard stock. The second approach would attempt to ensure more decentralized decision-making by allowing HOPEs to raise their funds directly.

As sponsors, the HOPEs would help or provide qualified home-buyers with financing, help them negotiate a fair price for their chosen house, determine that the house met proper standards, and assist at closings. Housing standards would be community standards meeting local housing and building codes but not necessarily FHA standards. The HOPEs would have the power to develop or rehabilitate housing on their own, in the same fashion that organizations under Section 235(j) currently do. They might act as organizers for the sale of group insurance contracts to cover monthly payments in cases of death, disability, fire, and perhaps loss of income due to unemployment, such as was envisioned in the study conducted in response to section 109 of the 1968 Housing Act.

In their direct lending program, HOPEs would utilize ownership, mortgages, and subsidies similar to FHA 235 but allowing more flexibility in types of houses. HUD could contract directly with a HOPE to guarantee the mortgages, to guarantee the subsidy in periods when needed, and to furnish the sums necessary for counseling and overhead of the HOPE. The individual insuring procedures, time, and expenses incurred under the present programs would be avoided. Control would be over the program in bulk rather than individual units.

As financial intermediaries, the HOPEs would contract with GNMA (or other HUD agency) which would guarantee payments on a pass-through mortgage bond used to raise funds for new or existing houses purchased by one or more HOPEs. Servicing of the accounts covered by the GNMA-backed bond could be handled by private mortgage servicing organizations as at present, under contract to the HOPEs. If the activities of a particular HOPE result in a significantly improved rate of successful housing experiences, consideration should be given to rewarding it with higher fees or a larger share of the total program.

In the appendix to this testimony, I discuss the possibility of utilizing such a program for a major saving in operating and subsidy costs. This is through the concept of loans rather than subsidies--a concept also applicable to existing programs. I believe substituting loans for subsidies would be sensible and proper. However, since these two ideas are more controversial than my basic proposal, I have placed them in the appendix to avoid any confusion.

The counseling available in a HOPE would go beyond simply helping the family find a home. It would offer a vehicle for all the elements which are currently envisioned in Title III of HR 9688 as necessary for successful home occupancy--advice on family budgeting, record-keeping, maintenance, and utilization of equipment--and perhaps go beyond where this is possible and desired, to family relations counseling.

Counseling can be one of the most important elements of success in this type of housing assistance. But it can also be the Achilles heel of the program.

The counseling program of the HOPE must avoid the obloquy that has fallen upon so much social work, however well intentioned. The home purchaser must not be made to feel that the price of the help he is receiving is constant prying into his affairs. He must not be subjected to humiliations arising from procedures suggesting that he is less reliable than other homebuyers, or that he is a statistical or social experiment. On the contrary, he must be treated with the same dignity and business-like courtesy that a conventional home purchaser receives from his mortgage banker.

On the other hand, there must be a recognition that the transaction is not a conventional one, that those purchasing homes on contract from HOPE have thinner resources than conventional homebuyers and that there are consequent obligations on both sides. I think this can be carried out without difficulty if the obligations are made clear from the outset, and if they are handled in a businesslike, rather than charity-like manner.

To the greatest degree possible, it should be the objective of the HOPE to leave homeowners to their own devices and depend for success upon the desire of most people to be successful and respected. Perhaps much could be learned from the procedures and traditions of the Agriculture Department's County Agents, and their relationships with their clientele, composed of highly independent-minded farmers who nevertheless can and do take advantage of a wide range of advice from their County Agent. The success of this agricultural counseling program demonstrates that a properly designed effort to transmit information to traditionally skeptical recipients can achieve outstanding results.

However, given the traditional distrust which many lower income families have towards any program which combines power (in this case, the power to evict a HOPE beneficiary from a home) with good intentions, it will probably be necessary, as I have suggested, to keep the counseling function of the HOPE at arm's length from the other functions. Thus, it would be advisable to have counseling services provided by subcontracting to community organizations. The counselors should always have the ability to act as the advocates of those who are supposed to be the beneficiaries of the HOPE program.

Why should it be thought that enterprises such as HOPEs will save money as compared to the current FHA programs? The Brookings Report on "Setting National Priorities - The 1972 Budget" (page 294) estimated subsidy costs could be cut in half solely through making the existing housing stock available for Federal housing assistance.

The reduction in subsidy costs would be aided by a major cut in operating costs (due to better use and maintenance of dwellings) and by the use of the entire housing inventory. Problems with the 235 and

236 programs arise because they have been thought of as specialized mortgage and construction programs--not as programs to improve a family's housing experience. They were grafted onto the existing FHA programs. No one is really responsible for seeing that existing subsidies are spent in an efficient and rational manner. Not surprisingly, the current technique of subsidy is expensive. Under current arrangements, turnover costs when a family moves may run 10 to 20 per cent if a family is successful and 30 to 40 per cent of the house value if there is a foreclosure. Since the programs are aimed at families in which turnover is expected to be high, these amounts will be equivalently high.

It should be clear that the funds made available to these enterprises would essentially parallel those in existing legislation, such as Section 237, or those proposed in Title III of HR 9688. I am primarily stressing the desirability of broadening the concepts of those proposals to increase the use of existing housing, to make available for subsidy all low-cost new housing, to cut losses and subsidies, and to make greater use of payments to the housing intermediaries, in accordance with performance.

Let me conclude, Mr. Chairman, by summarizing the main features of the HOPEs concept that would enhance the chances for success of the housing reforms your Subcommittee is considering:

1. HOPEs would be local and essentially non-governmental organizations.
2. They would constitute a one-stop housing service entity, not merely one more specialized housing institution.
3. The basic objective of the HOPEs would be to help a family match its housing needs (location, cost, tenure, and size) with the available stock.
4. It offers the promise of reducing the cost of subsidy programs through a higher rate of more successful housing experiences.
5. It promises to help prevent deterioration of the existing housing stock.
6. It provides for intensive, wide-ranging counseling services at the local level, free of government or establishment ties.
7. It is a logical vehicle through which the distinction--discussed in the appendix--between loans and subsidies could be tried.

APPENDIX:
TWO WAYS TO REDUCE SUBSIDY COSTS

Current housing subsidy programs require rapidly rising budget expenditures. The President's Third Annual Housing Report estimates that if the goal of 6 million subsidized units envisioned under the 10-year projections is reached, the yearly appropriations for these units by 1978 will have to be \$7.5 billion.

One way to reduce these costs would be to have the HOPEs in their direct lending programs hold titles to the houses as fiduciaries for the individual owners. Such a program would save large amounts in wasted financing, sales, and court costs and would, in addition, tailor subsidies to actual needs since these vary with changes in family incomes, changes in housing values, and in operating costs.

Under this type of operation, HOPEs, as fiduciaries, could also hold title to property sold under contract to cooperatives or other organizations sponsoring 236-type projects. If the owner failed to meet payments after all counseling efforts, and eviction became necessary, the HOPE would take possession of the property and offer it to another family. No foreclosure costs would be incurred. While the basic home-ownership objective of the HOPE would be the prevention of failures, it is reasonable to expect that failures will occur because of family problems, deaths, etc. By having the HOPE retain title to the property, the very high costs associated with foreclosures can be substantially reduced. Alternatively, the fiduciary relationship could be set up in a manner similar to that currently used in Section 235(j) arrangements, where a non-profit organization mortgages a group of dwelling units pending their resale to lower income families. In the interval, the organization is empowered to lease the units out. In the case of the HOPEs, the lease contracts could specify that a portion of the rental payments represented amortization of the mortgage, and at the end of a specified period, when the risk of foreclosure was reduced, title would pass to the occupant, along with full responsibility for maintaining the mortgage payments.

Secondly, the cost of any subsidy program administered by the HOPEs, as well as most existing housing subsidies, could be substantially reduced if the payments were treated as loans to be repaid, if possible, out of any increase in property values realized at the time of resale. In other words, monthly supplementary payments should be treated as take-downs against a government line of credit, rather than as outright, non-recoverable subsidy payments as is currently done.

An owner should have the right to convert his ownership of any type to a traditional fee simple with standard contract, or to sell it, at any time he pleases. However, when the property against which a subsidized mortgage is held is converted or sold, any capital gain (or some fraction of the gain) which accrues upon resale would be applied to

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reducing or eliminating the outstanding loan from the Government. Any gain in excess of the loan would go to the owner of the property. The loan would carry interest at the long-term government bond rate prevailing at the time the mortgage was originally made. If there were an insufficient gain (or a loss) on the property to retire the balance of the loan, any shortfall would automatically be written off by the Government as a subsidy, in much the same manner as the current system of farm subsidies operates.

There are two main advantages to this proposal over the current system of immediate, outright subsidies. First, a certain percentage of the money currently appropriated for outright subsidies would be eventually returned to the Government and available for further relending (or subsidy), with the probability that total program costs for subsidized housing would be reduced.

Secondly, it seems proper that the Government should be able to share in any gains which arise to homeowners and apartment investors by virtue of government contributions. The intent of the government subsidy programs is to provide adequate shelter to lower income families, not to finance speculation in real estate by investors or homeowners.

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**FUNCTIONAL DIAGRAM OF HOPE
RELATIONSHIPS**

