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The Troubled Dream: The Life and Times of Section 235 of the National Housing Act

by JOHN McCLAUGHRY*

PREFACE

I welcome John McClaughry’s analysis of the FHA’s section 235 home ownership program. His article is based on the report he prepared as a consultant to the Senate Government Operations Committee, on which I serve.

At the height of the controversy over the so-called “subsidized housing moratorium” announced in January, 1973, I recommended to Senator Sam J. Ervin, the Chairman of the Committee, that Mr. McClaughry evaluate the section 235 program, home ownership assistance for low and moderate income families. He had been my special assistant on housing when I drafted the National Home Ownership Foundation Act, one of several bills the Senate Committee on Banking and Currency considered in drafting section 235 of the National Housing Act, so I knew that he was uniquely qualified to examine the successes and failures of that program. I knew, too, that he would not hesitate to point out exactly where the fault lay for the problems which led to the 1973 moratorium.

Mr. McClaughry’s conclusions and his analysis of policy alternatives make valuable reading for anyone, lawyers and laymen alike, concerned about the future of federal housing programs. I agree with him that the 235 program compiled an enviable record of success even while being plagued by mismanagement. In my opinion, the National Home Ownership Foundation, had it been made operational after being

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authorized by the Congress in 1968, could have provided the oversight and direction necessary to avoid or quickly eliminate administrative problems as they arose.

That is in the past, however. The important point now is that we must apply in the future what we have learned from the history of the 235 program. Mr. McLaughry describes how this can be accomplished. I hope we pay heed.

SENATOR CHARLES H. PERCY
INTRODUCTION

In 1968, Congress, with considerable enthusiasm, enacted a major new program to enable lower income families to acquire the ownership of their own homes. Six years later, after an expenditure of $1.37 billion in assistance payments for over half a million families, the optimism of 1968 was thoroughly dissipated. Scandals and calamities had rocked the Department of Housing and Urban Development and its local Federal Housing Administration offices; FHA found itself the owner of record of tens of thousands of abandoned properties; the program itself had been suspended for 18 months; the Administration and Congress had clashed on the causes of the disaster; and everyone was more or less desperately looking for some way to deal with the emerging problems.

The 1973 program moratorium, the history of the 1968 HUD Act, the Moskow report, the Presidential Message of September, 1973, and the Housing and Community Development Act of 1974 are discussed, and eight conclusions reached as to the lessons learned to date from the whole experience. Five alternative strategies for dealing with the housing problems of lower income families are described in broad outlines, and a judicious mixture of four of them is suggested as a starting point for future policy.

THE GROWTH OF HOME OWNERSHIP PROBLEMS

"Home Ownership for the Poor," a rallying cry of 1967 in the battle to save the cities, has fallen upon evil times.2


Act contained new programs aimed at reaching the sweeping housing production goals proclaimed by President Johnson in his February 26, 1968, message to Congress on housing and the cities: 26 million new housing units, 6 million of them for low and moderate income families, over a 10 year period. This Act initiated a major new program for helping low and moderate income families to own their own homes. It also put Congress squarely on record in favor of relaxed FHA insurance requirements in declining inner city areas—the areas convulsed by the urban disorders of the mid-sixties.

Through January of 1974, 453,791 families had become homeowners under the new FHA section 235 home ownership program. Of these, 45,608 (10.05 percent) had been foreclosed, or their mortgages had been assigned to FHA for defaults. By contrast, as of 1973 the basic FHA 203(b), unsubsidized home ownership program had shown only a 2 percent rate of default termination. This higher rate of failure might not have been such an issue had not a combination of factors pushed the troubles of the FHA onto page one of the newspapers.

A Brooklyn grand jury in March, 1972, returned a 500 count indictment against 10 real estate corporations and 40 individuals, including 7 FHA employees. A Philadelphia grand jury later indicted 46 persons for similar offenses, including the former head of FHA's Philadelphia insuring office. The problems attracted a number of investiga-


gations, among them those of the Surveys and Investigations Staff of the House Appropriations Committee;\textsuperscript{12} the House Banking and Currency Committee;\textsuperscript{13} the Legal and Monetary Affairs Subcommittee of the House Government Operations Committee;\textsuperscript{14} the General Accounting Office;\textsuperscript{15} the HUD Office of Audit;\textsuperscript{16} and the Joint Economic Committee.\textsuperscript{17}

As a result of these disturbing events, HUD Secretary George Romney moved to tighten internal procedures. But at the same time, the Administration began to develop the position that the assisted housing programs adopted by Congress were inherently unworkable. Testifying before the House Housing Subcommittee on February 22, 1972, Secretary Romney said of the subsidized housing programs:

When I came in I had certain tools handed me and I used them. And I used them in the inner city. That is what [Congress] told us to do. Now, I am here today because it hasn't worked . . . . [W]hat you have asked me to do hasn't worked.\textsuperscript{18}

Two weeks later Secretary Romney carried this theme further. In a March 6 address to the National Housing Conference, he said of the subsidized ownership and rental programs:

This program was so poorly conceived and so uncautiously developed that we estimate the Federal government will in the next few years have more than 240,000 units in default—and with little resale value except at catastrophic levels of loss.\textsuperscript{19}

Finally, on January 5, 1973, the section 235 and 236 programs were


\textsuperscript{13} HOUSE COMM. ON BANKING AND CURRENCY, 91ST CONG., 2D SESS., INVESTIGATION AND HEARING ON ABUSES IN FEDERAL LOW AND MODERATE INCOME HOUSING PROGRAMS, Dec. 1970; bound in Hearing on HUD Investigation of Low- and Moderate-Income Housing Programs before the House Comm. on Banking and Currency, 92d Cong., 1st Sess. 99 (1971).

\textsuperscript{14} Hearings on Defaults on FHA Insured Mortgages before a Subcomm. of the House Comm. on Government Operations, 92d Cong., 1st & 2d Sess. (1971-72).

\textsuperscript{15} COMPTROLLER GENERAL, REPORT TO THE CONGRESS: OPPORTUNITIES TO IMPROVE EFFECTIVENESS AND REDUCE COSTS OF HOMEOWNERSHIP ASSISTANCE PROGRAMS (B-171630, Dec. 1972); reprinted in Hearings on Housing Subsidies and Housing Policies before the Subcommittee on Priorities and Economy in Government of the Joint Economic Comm., 92d Cong., 2d Sess. 46 (1972).

\textsuperscript{16} OFFICE OF AUDIT, DEP'T OF HOUSING AND URBAN DEVELOPMENT, AUDIT REVIEW OF SECTION 235 SINGLE FAMILY HOUSING (HUD Pub. No. 05-2-2001-4900, Dec. 10, 1972) (the findings are reported in OPPORTUNITIES TO IMPROVE EFFECTIVENESS AND REDUCE COSTS OF HOMEOWNERSHIP ASSISTANCE PROGRAMS; bound in Hearings on Housing Subsidies and Housing Policies, supra note 15, at 103).

\textsuperscript{17} SUBCOMMITTEE ON PRIORITIES AND ECONOMY IN GOVERNMENT, JOINT ECONOMIC COMMITTEE, 93D CONG., 1ST SESS., HOUSING SUBSIDIES AND HOUSING POLICY (1973).

\textsuperscript{18} Hearings on Real Estate Settlement Costs, supra note 4, pt. 1, at 286.

\textsuperscript{19} Address by HUD Secretary George Romney, National Housing Conference, March 6, 1972, quoted in Hearings on Defaults on FHA Insured Mortgages, supra note 14, pt. 3, at 488 (1972).
The action paralleled the Nixon Administration's impoundment of appropriated funds for many other domestic programs. Secretary Romney defended the action by observing:

It became crystal clear by 1970 that the patchwork, year-by-year piecemeal addition of programs over a period of more than three decades, had created a statutory and administrative monstrosity that could not possibly yield effective results even with the wisest and most professional management systems.

Speaking in President Nixon's name, White House assistant Kenneth R. Cole wrote Senator John Sparkman, Chairman of the Senate Banking Housing and Urban Affairs Committee:

The program structure we have now cannot possibly yield effective results even with the most professional management. There is mounting evidence that the present programs, for the most part, have proven inequitable, wasteful, and ineffective in meeting housing needs. They have proven inadequate and in most cases counter-productive in the greater solution of our urban and rural problems.

Members of Congress were quick to voice concern. In a stinging report issued on March 2, 1973, the majority of the Joint Economic Committee's Subcommittee on Priorities and Economy in Government concluded that "the primary problem with housing subsidies has been HUD mismanagement."

The subcommittee majority went on to say that:

The actions that have been taken, and similar announcements affecting many other programs, raise the most serious constitutional issue in many decades regarding our form of government. We recognize the need for some executive discretion in the management of Federal funds. But if the President can ignore the wishes of the Congress to implement programs for which it has

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20. The suspension was challenged in the courts by Pennsylvania, Maine and several nonprofit housing sponsors. In Commonwealth of Pennsylvania v. Lynn, 362 F. Supp. 1363 (D.D.C. 1973), the court held that the suspension was beyond the authority of the Secretary both in terms of the congressional mandate found in the statute and the constitutional duty of the executive branch to execute the laws. The court ordered HUD to resume processing applications.

21. For general discussion of the legal and constitutional issues raised by impoundment see Fisher, Presidential Spending Discretion and Congressional Controls, 37 LAW & CONTEMP. PROB. 135 (1972); Mills, Impoundment: A Search for Legal Principles, 26 U. Fla. L. Rev. 191 (1974); 23 CATH. U. OF AM. L. REV. 359 (1973); and 27 Rutgers L. Rev. 201 (1973). In 1974, Congress itself took action passing the Budget and Impoundment Control Act, Pub. L. No. 93-344 (July 12, 1974). The statute requires the President to notify Congress of any impoundment by special message. The executive decision to impound can be overruled by a simple resolution of disapproval by either house.

22. Address by HUD Secretary George Romney, National Association of Homebuilders, January 8, 1973, quoted in HOUSING SUBSIDIES AND HOUSING POLICY, supra note 17, at 3.

23. Quoted in HOUSING SUBSIDIES AND HOUSING POLICY, supra note 17 at 3.

24. HOUSING SUBSIDIES AND HOUSING POLICY, supra note 17, at 4.
Section 235 Housing

authorized and appropriated funds, by the unilateral gutting of programs, the power of Congress to raise funds for designated purposes has been destroyed. The elected representatives of the people will no longer have any power to decide upon priorities in the expenditure of Federal revenues which it alone can raise.26

In a Senate speech, Senator William Proxmire elaborated on this theme:

Section 235 housing has worked very well in some areas and not very well in others. But where it has failed, it has failed primarily because of bad, and sometimes criminal, HUD management.26

Joining in the debate, Senator Hubert Humphrey said:

The administration has indiscriminately characterized all our housing programs as ineffective, not serving the poor, and wasteful. They have made these assertions without evidence, and they keep repeating the assertions over and over again in the hope that they will be accepted.27

Thus, the Nixon Administration and Congress moved into a position of confrontation on yet another front. The Administration claimed that the present housing programs were unworkable, and unilaterally halted further program activity. Congressional leaders replied that the programs were well designed, and that the problems arose solely from mismanagement by the Administration.

Clearly, if the Administration position is correct, nothing short of a massive overhaul of federal housing programs is necessary. If the Proxmire-Humphrey position is correct, the programs are soundly conceived, and with capable management will attain their intended objectives.

THREE POSSIBLE STRATEGIES

To develop a balanced judgment on these competing claims, it is necessary to keep sharply in mind the policies underlying current and alternative home ownership assistance programs. Over the past six years three essentially differing strategies have been advanced to support the idea of expanding home ownership opportunities for lower income families.

The Individual Opportunity Strategy

This strategy recognizes home ownership as a worthy aspiration of Americans. It defines the problem as a denial of opportunity to some aspiring individuals: insufficient income to purchase a home, racial

25. Id. at 5.
27. Id. at S10,679.
discrimination that limits home selection, inability to manage credit, and limited capital in the home mortgage market. To help these worthy families become home owners, the Individual Opportunity Strategy calls for such federal policies as open housing, credit counseling for potential home buyers, an expansion of available mortgage credit, ending the artificial redlining of high-risk neighborhoods, and lowered costs of home purchase through subsidy. This strategy is not particularly concerned about where the new home owners purchase their home, so long as the opportunity for home ownership is opened for them.

The Production Strategy

This strategy focuses on increased volume of housing production as a primary goal. It defines the problem as artificial constraints on housing production, lack of large scale management capacity for home building, a shortage of mortgage money, and insufficient consumer demand for the new units to be produced. The Production Strategy calls for stimulating economic policies; rationalization and relaxation of building codes, work rules, and zoning requirements; the use of eminent domain for land assembly; production incentives; increased mortgage money through federal credit policies and institutions; and subsidies to enable more potential consumers to afford the costs of home ownership. The Production Strategy, like the Individual Opportunity Strategy, is not particularly concerned with where the new housing is to be built, and, all rhetoric aside, it is not so concerned about the housing plight of low income families as it is about a low number of housing starts. Nor is it particularly concerned about open housing, so long as high production is achieved; with high production the housing stock will increase and the poor will necessarily have a broader choice at prices they can afford, with or without subsidy. The Production Strategy is vocally advanced by such groups as the National Association of Homebuilders and the Mortgage Bankers Association.

The Neighborhood Strategy

This strategy begins with a concern about declining urban neighbor-

28. Redlining is the practice of marking a city map with a red line to indicate an area in which no further mortgage loans are to be made because of economic and physical conditions within the area. For further discussion of redlining by FHA see p. 14 infra; Testimony of Harold Greenwood, Hearings on Proposed Housing Legislation of 1967 before the Subcomm. on Housing and Urban Affairs of the Senate Comm. on Banking and Currency, 90th Cong., 1st Sess., pt. 1, at 500 (1967) [hereinafter cited as 1967 Senate Housing Hearings]; and Note, Redlining—The Fight Against Discrimination in Mortgage Lending, 6 LOYOLA U. CM. L.J. 71 (1975).
hoods. It seeks policies for preventing the decline of neighborhoods and revitalizing them as decent living environments. It recognizes that no housing policy alone can produce the desired result—that revitalizing a decaying urban neighborhood requires a full panoply of programs, public and private, to deal with the manifold problems of the slum: joblessness, dependency, alienation, powerlessness, poor education, insufficient municipal services, and poor housing.

The Neighborhood Strategy embraces policies that promise to mobilize the people in the neighborhoods to work together to preserve their neighborhoods. Chief among these is the promise of steady improvement in living conditions to the most capable neighborhood citizens, those who must provide essential indigenous leadership. Since neighborhood improvement is characteristically led by homeowners rather than tenants, creating opportunities for residents to acquire the ownership of decent homes is a key ingredient in this strategy. Other ingredients are public and private programs that motivate lower income residents to achieve, make available to them basic education, job training, and job opportunities, and generate mutual self-help efforts toward a wide variety of community goals.

The Neighborhood Strategy is not particularly interested in rural areas, for which the concept loses much of its meaning, or in open housing, or in massive housing production. It recognizes that many neighborhoods are too far gone to respond to a Neighborhood Strategy, and for these neighborhoods it has no well defined solution. Its goal is to provide the people of declining neighborhoods with the tools and the will to reverse the decline. Home ownership, associated with upkeep and retention of neighborhood leadership, is thus essential to success.

With this capsule summary of these three strategies, it is instructive to examine the genesis of the present 235, 223(e) and 237 programs, noting carefully which strategies underlay which legislative proposals, and how the rationales subtly shifted through the legislative process.

**GENESIS OF HOME OWNERSHIP ASSISTANCE FOR LOWER INCOME FAMILIES**

The year 1967 saw the emergence of home ownership for the poor

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29. The programs take their names from their respective section numbers in the National Housing Act of 1934, ch. 847, 48 Stat. 1246. Sections 235, 223(e), and 237 were added respectively by sections 101(a), 103(a) and 102(a) of the HUD Act of 1968, Pub. L. No. 90-448, 82 Stat. 477-85, 486, 485-86 (codified as amended at 12 U.S.C. §§ 1715z, 1715n, 1715z-2 (1970)).
as a national issue. The rioting in the nation's large cities, the well publicized Ribicoff subcommittee hearings on the crisis of the cities, the Kerner Commission study, and the innovative spirit of President Johnson's Great Society combined to focus the nation's attention on solutions to the problems of the slums.

A limited experimental FHA program had been enacted in 1966 under the leadership of Congresswoman Leonor K. Sullivan of Missouri. Tailored to meet the circumstances of an active slum improvement project in St. Louis, 221(h) provided FHA insurance for mortgages, initiated by nonprofit sponsors, on rehabilitated single family houses. Eligible home buyers could obtain a 3 percent, 25-year mortgage with a minimum $200 downpayment. Buyers' incomes were required to be lower than the income levels for continued occupancy of public housing in the locality. The program included a $20 million mortgage purchase appropriation to FNMA. Among the principal liabilities of the 221(h) program was its reliance on a below market interest rate, that made the resulting mortgages unmarketable and re-


32. Commonly known as section 221(h), the program was enacted as a part of the Demonstration Cities and Metropolitan Development Act of 1966, Pub. L. No. 89-754, § 310(a), 80 Stat. 1268-70 (codified at 12 U.S.C. § 1715f (1970)).

33. The Bicentennial Civic Improvement Corporation, St. Louis, Mo. The project is described in some detail in *Testimony of J.T. Dykman and Arnice Slaughter, 1967 Senate Housing Hearings, supra note 28,* pt. 2, at 974-82. *See also Mazer & Granat, Rehabilitation in St. Louis, 24 Journal of Housing* 200 (May 1967).


36. The below market interest rate had previously appeared as a feature of the rental property mortgages authorized by section 221(d)(3) in the Housing Act of 1961, Pub. L. No. 87-70, § 101(a), 75 Stat. 152. This section authorized the HUD Secretary to insure mortgage loans for rental housing for moderate income or displaced families at an interest rate as low as 3 percent or the current yield of outstanding Treasury obligations. In practice this became the "3 percent BMIR mortgage." Because of the below market rate, such mortgages could not be traded on the private market without enormous discounts. As a result, the Federal National Mortgage Association (after 1968 the Government National Mortgage Association) was forced to issue commitments to mortgagees to purchase BMIR mortgages at the mortgage closing, making the mortgagee merely a servicing agency instead of a lender. FNMA (GNMA) had to pay the full amount of the mortgage at its inception. This led to huge budget items and zero leverage of federal funds. Furthermore, to replenish its funds FNMA (GNMA) reported to the sale of participations in mortgage pools. Since the pools contained many mortgages at a below market interest rate, the selling agency lost money on every sale and was forced to obtain an annual insufficiency appropriation from Congress. This whole system became increasingly ridiculous and, by 1965, had led to a search for alternative means for injecting the federal subsidy.
quired a full-value budget expenditure to purchase every mortgage insured.

When President Johnson devoted only three lines to urban problems in his 1967 state of the Union message, a group of 28 Republican Senators, led by freshman Sen. Charles H. Percy of Illinois, issued a statement calling for "a new dawn of opportunity." Chiding the Democratic President for his virtual omission of the urban issue from his address, the Republicans offered three principles "on which a new national effort to bring dignity and a better life to today's slum dwellers must be based." These principles were:

1. harnessing the energies of private enterprise to the problems of the cities;
2. fostering self-help efforts by the people of the slums; and,
3. advancing home ownership for the "economically underprivileged," with its associated value of pride, dignity, and independence.

On July 17, 1967, major hearings began before the Senate Subcommittee on Housing and Urban Affairs, Senator John Sparkman, chairman. The Johnson Administration had submitted a measure making modest changes in a number of programs and offering as a response to the crisis of the cities only a new program for rat control. Others, however, both Democrats and Republicans, had offered creative new initiatives toward home ownership for the poor.

Senator Abraham Ribicoff (D-Conn.) offered a bill which would have created a new 3 percent BMIR mortgage for home ownership. This, he said,

would give families in this moderate income bracket a much needed and much deserved alternative—the opportunity to purchase a home of their choice that is within their means.

Senator Ribicoff's proposal clearly emphasized the Individual Opportunity Strategy, placing no emphasis on overall housing production and requiring no neighborhood focus. At the same time, interestingly enough, he also sponsored S. 1433, the Neighborhood Development

37. 113 Cong. Rec. 36 (1967).
38. 113 Cong. Rec. 1523 (1967).
39. Id. at 1524.
40. Id.
41. 1967 Senate Housing Hearings, supra note 28.
44. 1967 Senate Housing Hearings, supra note 28, pt. 1, at 288.
Corporation Assistance Act, a bill based squarely on the Neighborhood Strategy. It would have required the Secretaries of HUD, Commerce, Labor, and HEW, and the Director of OEO, to study

the most practicable ways to coordinate the activities of neighborhood development corporations with federally assisted programs and activities for improving housing conditions, increasing employment and business opportunities, expanding worker productivity through job training and education.

The two Ribicoff bills were, however, totally independent of each other.

Senator Charles Percy, with 39 Senate co-sponsors and 112 House sponsors, led by Rep. William B. Widnall of New Jersey, offered the National Home Ownership Foundation Act, S. 1592. This bill, exemplifying the Neighborhood Strategy, would have chartered a quasi-public National Home Ownership Foundation. The bill had these main provisions:

1. federal assistance to lower income home buyers to help them pay the costs of their mortgages—the payments would be made directly by the Treasury to the mortgagee through a "coupon mortgage;" as a home owner's income rose, the government payment was reduced by means of an income tax recapture provision; this financial device obviated the need for subsidy via a BMIR mortgage;

2. a Home Ownership Loan Fund, capitalized at $2 billion through the public sale of federally guaranteed debentures, to provide necessary mortgage capital;

3. a Technical Assistance Service to assist neighborhood nonprofit groups to organize and conduct broad-based home ownership programs, including generating widespread participation by business, labor, churches, colleges, and government agencies; funding the elements of a housing construction or rehabilitation program; training local people in program management; and obtaining access to supporting programs in the fields of training, employment and counseling and other related programs necessary to the success of a home ownership program.

S. 1592 called for a 3 year authorization of $60 million in mortgage

46. Id. at § 5(b).
payment support. It was estimated that this amount would produce some 200,000 housing units over a 3 year period. Senator Percy also proposed a number of options to the workings of the proposed Foundation.\textsuperscript{48}

The Percy-Widnall bill, which limited its assistance to neighborhood organizations attacking neighborhood problems along a broad front, was squarely based on the Neighborhood Strategy. While supportive of the Individual Opportunity Strategy in part, the bill did not contemplate financing the out-migration of the most affluent families from a declining neighborhood. The bill did attempt to give these families an incentive to stay and devote their talents to neighborhood revitalization. Its goal of 200,000 units over 3 years was timid in comparison with President Johnson’s 1968 goal of 6 million subsidized units over a decade; Senator Percy recognized that the lack of a strong neighborhood infrastructure would limit his bill’s utility to a far lower figure.

The third major home ownership bill to be introduced was S. 2115,\textsuperscript{49} by Senator Joseph Clark (D-Penn.). The purpose of S. 2115 was to provide mortgage insurance for persons whose credit histories precluded insurability under current FHA home mortgage programs. The bill permitted FHA to insure mortgages for persons with a poor credit history and fluctuating incomes, provided such persons were given budget, debt management and related counseling services. Mortgages insured under this new section were to be assigned to a new Special Insurance Fund, and would thus not threaten the fiscal integrity of the regular FHA reserve funds. The new fund was to be capitalized by a direct $15 million appropriation, instead of through the payment of mortgage insurance premiums as in the standard FHA section 203 program.\textsuperscript{50}

Senator Clark’s bill was also an Individual Opportunity bill. It had been inspired by a HUD-sponsored, low income housing demonstration project in Gainesville, Florida.\textsuperscript{51} Project sponsors found that many families were needlessly barred from home ownership by dubious credit reporting practices, and that, with proper counseling and assistance, these families could become responsible homeowners. The Clark bill did not carry a subsidy, other than the waiver of the $\frac{1}{2}$ percent mortgage insurance premium.

\textsuperscript{49.} S. 2115, 90th Cong., 1st Sess. (1967).
\textsuperscript{51.} For a description of the Gainesville project see \textit{Testimony of Gloria Richards and Phillip Emmer}, 1967 Senate Housing Hearings, \textit{supra} note 28, pt. 1, at 825.
Senator Walter F. Mondale (D-Minn.) offered another home ownership bill, S. 2124.\textsuperscript{52} In essence, it was a combination of Senator Ribicoff's home ownership bill, Senator Percy's financial mechanism, and Senator Clark's special risk insurance fund, applied to existing housing only. Under S. 2124, an eligible "person of modest means" could obtain a home mortgage by paying the equivalent of 3 percent interest while the FHA made the required supplementary payment to the mortgagee to make up the full market interest rate. The mortgages would be assigned to a special "home purchase insurance fund" backed, if necessary, by appropriations instead of premiums. The bill authorized $50 million in mortgage payment assistance over 2 years, and up to $200 million in FNMA purchase authority to ensure a strong secondary market for the new mortgage instrument.

Senator Mondale stated that his bill aimed at dealing with "the dual problem of the high cost of credit and the scarcity of mortgage money for lower priced housing."\textsuperscript{53} He explicitly rejected the Neighborhood Strategy,\textsuperscript{54} and his authorization levels, coupled with the restriction to existing housing only, implied a rejection of the Production Strategy as well. Like the Ribicoff and Clark bills, the Mondale bill was principally an Individual Opportunity bill.

In addition to considering these various measures for encouraging home ownership among low and moderate income families, the Housing and Urban Affairs Subcommittee members became increasingly concerned about the redlining of declining urban areas by both FHA and private lenders.\textsuperscript{55} Historically, in its popular 203 ownership\textsuperscript{56} and 207 rental\textsuperscript{57} programs, FHA had by law been required to apply a test of "economic soundness" in insuring mortgages. This test basically related to the location of the proposed unit. To pass the "economic soundness" test, the neighborhood had to exhibit market acceptability in terms of future viability and stability. Slum areas and rapidly changing urban neighborhoods could not meet the test, and it was these areas which were redlined by FHA and private lenders alike.\textsuperscript{58}

\textsuperscript{52} S. 2124, 90th Cong., 1st Sess. (1967).
\textsuperscript{53} 1967 Senate Housing Hearings, supra note 28, pt. 1, at 476.
\textsuperscript{54} Id. at 480.
\textsuperscript{55} See note 28 supra.
\textsuperscript{57} National Housing Act Amendments of 1938, ch. 13, § 4, 52 Stat. 18 (codified as amended at 12 U.S.C. § 1713 (1970)).
\textsuperscript{58} For background see generally HISTORY OF RISK CONCEPTS IN HOME MORTGAGE INSURANCE LEGISLATION, in HOUSE COMM. ON GOVERNMENT OPERATIONS, DEFAULTS ON FHA INSURED HOME MORTGAGES—DETROIT, MICHIGAN, H.R. REP. NO. 92-1152, 92d Cong., 2d Sess. 51-56 (1972).
Two steps had previously been taken to relax the "economic soundness" criterion in certain instances. The section 220 program, enacted in 1954, allowed the substitution of an "acceptable risk" criterion in place of "economic soundness," and the use of "replacement cost" instead of "value" in appraising insured properties. The 220 program was available only in urban renewal and concentrated code enforcement areas, and was justified by the anticipated restoration of those areas to decent living environments and viable mortgage markets. In 1966, Congress also enacted a new section 203(l) mortgage insurance program which substituted "acceptable risk" for "economic soundness" in riot-prone areas. This section was only sparingly used before its repeal by the HUD Act of 1968.

The Senate Subcommittee in 1967, in the omnibus bill ultimately reported to the Senate, included a new section 223(e), that substituted "acceptable risk" for "economic soundness" in "reasonably viable" inner city areas, "giving consideration to the need for providing adequate housing for families of low and moderate income" in such areas. Claims arising from mortgages insured under section 223(e) were to be paid from a special risk insurance fund created by the 1967 Act.

As the Housing and Urban Affairs Subcommittee completed work on the 1967 Housing and Urban Development Act, a significant development took place at HUD. On October 23, 1967, FHA Director Philip N. Brownstein delivered a celebrated address to FHA directors and underwriters. Apparently stung by the criticism of FHA for redlining inner cities, and fearful of congressional action to establish a parallel home mortgage insurance program outside FHA, Brownstein issued a stirring mandate to his administrators:

We have got to recognize that stimulating a flow of mortgage funds into the inner city, yes, even the slums, for the transfer of houses, for rehabilitation, and for new construction, is an FHA mission of the highest priority. No longer can we afford to wait until an applicant comes in and bludgeons us into this kind of activity.

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63. Id. § 103.
We must be willing to take the risks necessary to accomplish the urgent job of assisting and encouraging private enterprise to house low- and moderate-income families and to revive the inner city. It is highly likely that there are more risks inherent in achieving this kind of urgent social purpose than in the insurance of loans on suburban subdivisions.

. . . I am asking you and every employee of FHA to enter into a new crusade—to see that our programs are used to the fullest extent possible to improve housing conditions for low- and moderate-income families and to revive the inner city.64

This address signaled a major broadening of policy at FHA: from suburban-only insuring and a defense of its reserve funds to a new emphasis on inner city involvement at admittedly higher risk.

On November 28, the Senate Banking and Currency Committee reported a clean bill to the Senate.65 The bill included these major provisions:

1. a home ownership assistance program, designated section 235 of the National Housing Act, that authorized HUD to pay to section 235 mortgages a monthly payment sufficient to produce the equivalent of a 3 percent mortgage to the home buyer;66

2. a rental assistance program, designated section 236, to make equivalent subsidized housing available on a rental basis;67

3. a Special Risk Mortgage Fund, not designed to be actuarially sound through the payment of mortgage insurance premiums, to which the new section 223(e), 235, and 236 mortgages would be assigned;68

4. a relaxation of the "economic soundness" mortgage insurance criterion in older, declining urban areas, in favor of a doctrine of "acceptable risk" in view of the need for low and moderate income housing in those areas;69

5. loans and technical assistance to nonprofit housing sponsors;70

6. miscellaneous studies, commissions, and housekeeping amendments, including a National Home Ownership Foundation lacking any clear-cut function.71
Thus reported, the home ownership provisions of S. 2700 were based squarely on the Individual Opportunity Strategy. The scope of the proposed 235 program was limited: 200,000 units over 3 years, as proposed in Senator Percy's bill. The authorizations for mortgage payment assistance were $10 million in Fiscal Year 1968, $35 million in Fiscal Year 1969, and $70 million in Fiscal Year 1970. The only Production Strategy ingredient evident in S. 2700 was the requirement that, with the exceptions of public housing residents, families with five or more children, or displacees, none of the proposed payments could be made with respect to existing housing.

The Senate did not, however, act on the proposed Housing and Urban Development Act of 1967. Instead, it waited for President Johnson's message on the problems of the cities, which arrived on February 26, 1968.

The President's message proposed a program of federal assistance for the construction and rehabilitation of 6 million housing units over a 10-year period for the low and moderate income families as a part of the goal of 26 million overall housing units to be produced during this same 10-year period. This ambitious goal contrasted sharply with the actual number of publicly assisted housing units built in immediately preceding fiscal years: 1966, 49,000; 1967, 57,000; 1968, 128,000. The President was placing the emphasis on a Production Strategy.

On May 15, 1968, the Senate Banking and Currency Committee reported a new committee bill, S. 3497. In so doing the committee had obviously adopted a strong emphasis on production. With respect to the home ownership provisions, the 1968 bill, as passed, increased the first year authorization from $10 million to $75 million; the second year from $35 million to $175 million; and the third year from $70 million to $300 million, compared to the authorizations in the 1967 bill. In addition, the new bill deepened the interest subsidy from 3 percent mortgage payments to 1 percent mortgage payments, thus enlarging the number of potential homeowners significantly.

References:
73. Id.
74. Id. at 9.
75. Crisis of The Cities—Message from the President of the United States, 114 CONG. REC. 3956 (1968).
79. Id. § 101(a), 82 Stat. 478.
The Johnson Administration had pressed for an even larger clientele for the new home ownership and rental program. When the committee proposed to limit eligibility to income levels not in excess of 70 percent of the local 221(d)(3) income levels, HUD Secretary Weaver objected on the grounds that "by having the more liberal upper limits, you have the possibility of getting a greater volume quicker." In the final version, the level was set at a more liberal 90 percent of the 221 (d)(3) levels.

The Senate bill, which was to become the Housing and Urban Development Act of 1968 without major change, thus superimposed a strong Production Strategy approach on the Individual Opportunity approach of the previous year. The Neighborhood Strategy was abandoned precisely because it was incompatible with a Production Strategy. If the new programs were to be available only in neighborhoods that had formed a housing corporation and had begun comprehensive and expensive efforts to upgrade not only housing but also the living environment and the life opportunities of the residents, then it was clearly impossible to attain anything like the national housing goals proposed by the Johnson Administration.

This rejection of the Neighborhood Strategy was peculiarly ironic in that Secretary Weaver had attacked the Percy proposal on the grounds that it did not adequately integrate and coordinate a wide variety of neighborhood improvement programs nor sufficiently involve local governments. Whatever the merits of the Secretary's attack on the Percy-Widnall proposal, this much was absolutely certain in 1968: the

81. In a release dated April 21, 1967, the day the Percy-Widnall bill was introduced with wide sponsorship and publicity, Secretary Weaver issued a statement which said:

The failure of the proposal to involve local government means that it cannot become a major instrument for revitalizing urban slums and blighted areas. . . . The local governing body has to be involved in any large scale attempt to improve neighborhoods. . . . The failure of the proposal to involve local government may result in the activities actually harming a local community's plans for its redevelopment or growth.

Soon thereafter, in a radio interview, the Secretary described the proposal as a "snare and a delusion":

To promise large numbers of low income people that in the immediate future they are going to be able to achieve home ownership is a snare and a delusion and it can be a cruel hoax because in many instances with these extremely low down payments, with these long periods of loans after three years they will have a negative equity. And if they lose their jobs, or if they are sick, they will lose their home. . . .

After describing his department's experimental work with the 221(h) program, Secretary Weaver added:

We are tying this to other programs, as contrasted to the Percy program which would be out there by itself and would not be coordinated with all that's going on.

These statements were reprinted at 113 CONG. REC. 18,036-37 (1967).
HUD Act of 1968 initiated a program to help far poorer home owners than Senator Percy’s bill; it omitted any connection with local government or other public programs to help the homeowners advance economically; and it contemplated a program five times as large as the one offered by Senator Percy.

While ardently supporting the 1968 bill, Senator Percy expressed his deep concern over the committee’s abandonment of what he termed the “integrated approach”—dealing simultaneously with both people and housing problems. In individual views on the 1967 bill, the Illinois Senator observed:

Merely installing lower income families in decent structures that they own may well not, absent other considerations, result in the achievement of the goals of this program. Lower income families need the education and training that leads to decent jobs and advancement up the job ladder. They need instruction in the intricacies of mortgage financing, consumer buying, insurance and taxes, home maintenance, and community participation that accompany effective home ownership. Unless these factors are fully taken into account, the result may only confirm the fears of the skeptics in HUD and elsewhere that lower income families do not have the capacity to sustain home ownership, but must remain perpetual wards of the public housing agency or tenants of a benevolent landlord.82

Senator Percy’s 1967 fears were to prove prophetic.

In addition to the foregoing provisions, the HUD Act of 1968 enacted a new section 237 of the National Housing Act,83 providing for the insurance of mortgages to low and moderate income home buyers who, with counseling assistance, could overcome poor credit history and irregular income patterns to qualify. This provision, originally Senator Clark’s bill,84 had not been included in the 1967 omnibus bill. Strangely, the counseling assistance authorized under section 237 was not initially directed to regular 235 home buyers, who might be expected to need it most. It was not until the Housing and Urban Development Act of 1969 that section 237 was amended to explicitly authorize HUD counseling to 235 buyers.85

In summary, the home ownership provisions of the HUD Act of 1968 had these characteristics:

1. The Act created a major new program of subsidized mortgage insurance to help lower income families become home owners. The section was based on the Individual Opportunity approach, on which had been superimposed a very strong Production emphasis.

2. The terms of the new program made it possible for hundreds of thousands of families to qualify for home ownership by lowering the effective mortgage interest rate to 1 percent, with minimal down payments and long mortgage terms. The income eligibility levels had been raised, generally, to 90 percent of the moderate income 221(d)(3) program to increase the universe of eligible home buyers at the high end of the scale, just as the availability of 1 percent money increased it at the lower end of the scale. Both of these actions were necessary to create enough eligible buyers to make the production goals attainable.

3. The new program was made available to home buyers with absolutely no regard to any neighborhood organization, nonprofit sponsor, housing authority, or local government body with a continuing concern for the preparation and protection of the unsophisticated buyer. The counseling provisions authorized under the new section 237, moreover, were not directed to section 235(i) home buyers.86

4. The traditional "economic soundness" standard for mortgage insurability, relating to the location of the house in a neighborhood of stable or rising property values, was abandoned in favor of an "acceptable risk" standard, which, coupled with FHA Commissioner Brownstein's urgent exhortations,87 virtually forced FHA into previously redlined areas.

5. By establishing a Special Risk Insurance Fund, section 238, Congress for the first time initiated a mortgage insurance program not designed to be actuarially sound over the long run, and separated it from the traditional FHA insurance funds. By this action, FHA's jealous protection of its reserves was made far less important than previously, and consequently FHA was encouraged to embark on higher risk programs.

Under these terms, a poor person who had never before been able to buy a home became a potential home buyer; no counseling or community support was available to help him understand this new proposi-

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86. In fact, no funds were appropriated for this purpose until Fiscal Year 1972.
87. See note 64 supra.
tion; previously shunned areas were now opened up for FHA insurance; FHA was given a mandate to reverse its past policies of inner city caution; and the President and Congress had subscribed to a drastically increased production level of subsidized housing. This combination of factors pointed directly to trouble.

THE HOME OWNERSHIP PROGRAM IN OPERATION

The new home ownership programs were enthusiastically received by builders, brokers, and mortgage financiers, as well as by many lower income families. The procedure was simple: the prospective home buyer located a home, either existing, rehabilitated, or new; went to FHA for mortgage insurance, closed the loan with the bank, and became a homeowner. Builders, brokers, and sellers regularly scouted up prospective lower income families, peddled homes to them, and made their profits.

In many cases, of course, everyone was happy with the sale and the new homeowner made his payments regularly. Not infrequently, however, things did not go so smoothly. In a typical case, a real estate operator would buy up a number of run-down or abandoned buildings in an inner city slum. He would make sufficient cosmetic repairs to make the building temporarily presentable. A FHA appraiser—often a fee appraiser—would inflate the appraisal value, occasionally for an illegal kickback. The operator would find an aspiring low income family with little knowledge of the responsibilities of home ownership. The bank would make the loan, knowing, of course, that FHA would step in in case of default. The operator would take his money and disappear. Later, the homeowner would discover that his home had many substandard conditions—conditions more expensive to correct than his limited budget permitted. Having only some $200 in the deal, and facing huge expenses and protracted wrangling, the homeowner would abandon the property and disappear. And another problem home went into the FHA inventory.88

The most spectacular disaster occurred in Detroit. There, in Secretary Romney's words:

FHA personnel were encouraged to begin to do what they had not been doing; namely, to put families into homeownership situations in the central city in areas that had previously been red-lined.

This was undertaken by personnel that had previously been putting middle-income families into homeownership situations in the

88. See generally Shah, Housing Mess, supra note 11.
suburbs who have mortgage insurance, but not families with problems of the type encountered in the central city and not in an environment of the type encountered in the central city and they were putting them into new homes more than existing units.89

By May, 1972, the General Accounting Office had reported to the House Government Operations Committee's Subcommittee on Legal and Monetary Affairs that:

Acquisitions of property insured during 1968 [in Detroit] have reached alarming proportions. More significant, however, is the fact that acquisitions of property insured during 1969 and 1970 are following the same trend. For example, as of February, 1972, the acquisition rate for houses insured under the 223(e) program during 1968 has reached 34.6 percent and is still climbing; the rate for houses insured during 1969—1 year later—is already 26.4 percent and climbing; and the rate for houses insured during 1970—2 years later—is already 11.6 percent and climbing. Only time will tell what the ultimate rate will be.90

The GAO investigators estimated that when the FHA-owned properties in Detroit were completely sold or razed, the total loss to the FHA would run as high as $200 million. This estimate apparently did not take into account the further difficulties experienced in the Detroit office due to the tremendous unexpected volume of acquisitions and liquidations. This high volume, handled without significant staff increases, so disrupted the routine operations of the FHA office that "normal" FHA 203 acquisitions, usually at the 2 percent level of insurance in force, could not be handled properly. In many desirable areas of the city, $35,000 houses stood vacant until they were vandalized, merely because of the congestion caused by the inner city crisis.91

The causes of the increased foreclosures in Detroit, according to the House Subcommittee, were: overpriced and structurally unsound houses; unsophisticated home purchasers; a failure by the state of Michigan to properly regulate the real estate industry; failure of FHA and FNMA to curb imprudent lending by mortgage companies; failure by HUD to screen and counsel inner city home buyers; inadequate HUD staffing; lack of interagency coordination; and a desultory approach to prosecution of lawbreakers.92

Other investigations had reached similar conclusions about the home ownership programs in general. The December, 1971, report of the HUD Office of Audit\(^9\) cited defective appraisals, inadequate internal supervision, lax penalty procedures, and inadequate handling of complaints by home buyers. These problems, said the report, were caused by "the attitude of certain HUD-FHA personnel, including management, supervisory and line staff, regarding the socio-economic aspects of the program;"\(^9\) the quality and quantity of appraisals, and poor middle management.

In a more formal investigation of the entire home ownership program, the General Accounting Office recommended reinspection of all houses within the 1 year warranty period after purchase, a new effort to link program resources to needs, and additional study of defaults to aid screening and counseling programs.\(^5\) In addition to these reports, Secretary Romney and his staff were subjected to intensive interrogation by the Appropriations Committees of both House and Senate in 1971 and 1972.\(^9\)

In a candid statement before the House Banking and Currency Committee on December 16, 1970, Secretary Romney outlined the genesis of the debacle: "Faced with a housing shortage of crisis proportions, in the teeth of the worst credit crunch and housing shortage since World War II . . . we pushed the 235 program and all our assisted housing programs to the limit."\(^9\) Citing a growing involvement of FHA in inner city problems since 1965, and particularly since 1968, the Secretary observed that "neither FHA nor anyone else had an adequate understanding of the problems inherent in an effort to place low-income families in a homeownership situation."\(^9\) The combination of high production goals, the relaxation of the "economic soundness" doctrine in inner cities, the availability of 1 percent mortgages under 235, the special risk fund without a requirement of actuarial soundness, and the congressional mandate to accord "a preference to those families

\(^9\) AUDIT REVIEW OF SECTION 235 SINGLE FAMILY HOUSING, supra note 16.
\(^9\) Id. at 5.
\(^9\) OPPORTUNITIES TO IMPROVE EFFECTIVENESS AND REDUCE COSTS OF HOME OWNERSHIP ASSISTANCE PROGRAMS, supra note 15, at 33, 39, 45.
\(^9\) Hearings on HUD Investigation of Low- and Moderate-Income Housing Programs, supra note 13, at 234.
\(^9\) Id. at 237.
whose incomes are within the lowest practicable limits for achieving homeownership with assistance under this section”99 taken together with virtually no increase in FHA staff, could hardly fail to produce a serious default problem.

Despite this relatively early recognition of problems, and despite numerous internal steps to tighten up the program, things had scarcely improved by April 10, 1972, when Secretary Romney told the House Appropriations Committee:

These changes in the rules and procedures under which FHA had operated for years brought—along with some substantial successes—some unexpected and damaging results.

These unexpected problems and their potential, I regret to say, were not apparent when I became Secretary of Housing and Urban Development in January, 1969. The problems we tackled immediately were of a different character. Housing production was declining. Housing costs were soaring. Mortgage money was in short supply. Congress had set an ambitious goal in the 1968 Housing Act, calling for production of 26 million housing units—6 million of them for low and moderate income families—by 1978.

I concentrated on solving these problems. In retrospect, it was a mistake—in part—not to realize that the FHA was not prepared for its new role in central cities and its exposure to speculators and fast-buck artists.

There was practically no preparation for this fundamental change [at FHA]; as a matter of fact, it occurred when FHA was least prepared for it.100

As a temporary emergency measure, Secretary Romney suspended approvals of all pending applications for section 235 existing home financing in early 1971. As internal changes were made in various insuring offices, this suspension was lifted. On January 8, 1973, however, the Administration announced suspension of all section 235 activity for a period of 18 months, ostensibly to give the Administration time to propose alternative methods of meeting the low income housing problem.101 The Administration, however, was not too explicit about why,
after 3 full years of rising costs, front page scandals, and congressional investigations of the low income housing program, plus an almost annual confession of sins by the responsible cabinet officer, it had not been able to generate any alternative ideas. There was considerable reason to believe that overall budget considerations had a great deal to do with the “necessity” of the suspension.\footnote{102}

**Counseling**

In one particular FHA office—Milwaukee—the results of the 235 program had been spectacularly gratifying. Under the leadership of Director Lawrence Katz, as of early 1972 the Wisconsin FHA area had a record of only nine foreclosures out of 8500 mortgages insured under sections 235 and 237—a .09 percent foreclosure rate. “The secret of Wisconsin’s success has been to mobilize every conceivable national, State and local, public and private ally, in a well-coordinated blitz on the barriers to upward mobility of the poor,” according to a report prepared by the Mortgage Bankers Association.\footnote{103}

In Milwaukee, the program worked as follows:

The applicant, frequently a welfare mother, must attend three pre-purchase counseling classes in which two FHA staffers explain taxes, insurance, amortization and the buyer’s responsibility. Graduates are then told: “You are on your own. Find a house and talk to a real estate broker.” FHA has a list of brokers and properties.

If the applicant doesn’t have the required $200 minimum downpayment, the St. Vincent dePaul Society will provide it from a $100,000 fund for downpayment grants.

The buyer selects a house, and the county welfare agency checks its condition and adequacy. One of the 12 welfare agency housing aides then may certify approval of the structure.

The welfare agency’s approval triggers the standard FHA inspection. If FHA approves, they notify the St. Vincent dePaul Society to release the downpayment, if needed.

\footnote{102. *Hearings on Oversight on Housing and Urban Development Programs before the Subcomm. on Housing and Urban Affairs of the Senate Comm. on Banking, Housing and Urban Affairs, 93d Cong., 1st Sess., pt. 1, at 2 (1973).*}

\footnote{103. *Hearings on HUD-Space-Science-Veterans Appropriations for 1973, supra note 12, pt. 3, at 1515. This was precisely the approach advocated by Senator Percy’s 1967 legislation. For example, section 110(a)(2) of S. 1592 required that the neighborhood housing sponsor, to qualify for a mortgage loan, “must be conducting, or otherwise arranging for, supporting programs in such fields as training, employment, credit counseling and budget management as needed to enable lower income families to assume the privileges and responsibilities of homeownership.” This integrated approach, as a basic part of a Neighborhood Strategy, was rejected in the HUD Act of 1968. See discussion *supra* at pp. 17-18.*}
Five days before closing, the buyer goes to the property, examines its condition and signs an acceptance that lists anything he does not like about the condition. This is important where there was no model home to inspect.

Next, a voluntary group of lawyers operating under an OEO program is cranked into the procedure, to represent the buyer at settlement.

After purchase, the buyer goes to classes in home maintenance conducted by the Milwaukee County Welfare Department, and is paid $53 a month for 2 months' attendance. The buyer receives transportation and is provided nursery services to look after the children while in class. The University of Wisconsin's extension program assists the program with a select group of welfare mothers, previously counseled in 235 ownership, as team leaders. The buyer is taught to replace faucet washers and fuses, how to upholster, make drapes, and purchase groceries wisely.

At the end of the course, the buyer gets his choice of $65 worth of tools provided from a government grant to the University of Wisconsin.

Since the Welfare Department has financial exposure (when they endorsed the house prior to purchase, they guaranteed to take care of all major and minor repairs that the buyer cannot make) a welfare aide returns for inspections scheduled every 3 months to spot neglect that might cause serious deterioration.

Costs incurred in this program are shared 55 percent by the Federal Government (OEO), 27.5 percent by the State and 17.5 percent by the county.104

Ironically, for his careful work to achieve both the goals of lower income home ownership and expanded production, Katz became the "bad boy" of FHA.105 His "body count" of housing was too low. At the same time, the Detroit FHA director was getting rave reviews106 for his aggressive processing of inner city homes, the subsequent results of which are now well-known.

The success of section 235 for welfare mothers in inner city Milwaukee is a testament to the importance of counseling. In his statement before the House Banking and Currency Committee on March 31, 1971, Secretary Romney observed that "neither FHA nor anyone else had adequate understanding of the problems inherent in an effort to


place low income families in a home ownership situation." This statement was demonstrably untrue.

During the Senate Housing and Urban Affairs Subcommittee's deliberations on what became the HUD Act of 1968, a host of witnesses came at Senator Percy's invitation to describe their work in helping low income families become home owners. Among these were the representatives of the Bicentennial Civic Improvement Corporation of St. Louis; the Interfaith Interracial Council of the Clergy in Philadelphia; the Board for Fundamental Education in Indianapolis; Lincoln Estates of Gainesville, Florida; Better Rochester Living, of Rochester, N.Y.; HOPE, Baltimore; along with many other experts with practical experience in housing lower income families. Even HUD Secretary Robert C. Weaver placed a strong emphasis on this point, saying in 1967:

Under favorable circumstances, an effective neighborhood development effort can utilize housing and neighborhood rehabilitation as an instrument for reversing the cycle of poverty. Home ownership can be an important element in that total effort. But without such a comprehensive and coordinated attack for reversing that cycle, homeownership alone will often be doomed to failure.

HUD had, in fact, funded a number of low income housing demonstration projects, notably in Gainesville, Florida, San Francisco, California, and Tulsa, Oklahoma, specifically aimed at shedding light on the essentials of lower income home ownership. In addition, the Senate Report on the HUD Act of 1968 stated:

Since many of the families who would be assisted have had little experience in the proper care of a home and the budgeting of income to meet regular monthly payments on a mortgage, this section would authorize appropriate counseling, either directly by HUD or by contract with public or private agencies, to assist these families in meeting their new responsibilities. Appropriations would be authorized for this purpose.

In his individual views on S. 3497, Senator Percy once again observed:

The credit assistance and counseling provided in the bill are essential to a successful home ownership program. It is vital that

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107. Hearing on HUD Investigation of Low- and Moderate-Income Housing Programs, supra note 13, at 237.
109. Id. pt. 1, at 9.
In Fiscal Years 1970 and 1971, HUD requested an appropriation to implement the counseling authorized under section 237, which had been made the vehicle for section 235 counseling by the Housing and Urban Development Act of 1969. Each year HUD was rebuffed by Congress. Denying HUD’s plea for $3.1 million in Fiscal Year 1971, the HUD Appropriations Act directed HUD to use existing departmental funds for any program to be developed. As a result of these two rebuffs, HUD did not request counseling funds for Fiscal Years 1972 and 1973.

Instead, HUD initiated two different unfunded counseling programs. Under section 237, HUD was forced to rely on unpaid voluntary organizations to counsel families with poor credit ratings, to enable them to qualify as section 235 homeowners. In addition, HUD developed a pilot program in 15 selected cities where $100 was withheld from the mortgage proceeds due the seller. This $100 was paid, if necessary, to a local counseling organization to prepare the prospective homeowner for the responsibilities of ownership.

In Fiscal Year 1972, somewhat to HUD’s surprise, Congress volunteered a $3.25 million appropriation for home ownership counseling. HUD hastily put a group to work on ways of using the funds. In 1970, the last year that HUD had requested appropriations for counseling, a small contract program with a central office staff of five was presented to the appropriations committees. In 1972, however, the HUD working group proposed a program which would have, in Secretary Romney’s words, built “quite a sizeable organization.” Romney vetoed the plan, with the result that HUD just barely managed to obligate most of the $3.25 million in Fiscal Year 1972.

112. Id. at 204.
118. Id.
HUD used the Fiscal Year 1972 funds to set up a "Counseling Fee System Demonstration" to offset the administrative costs of local counseling agencies in the 15 pilot cities. The contracts were let in June, 1972. HUD did not request a further appropriation for Fiscal Year 1973, stating that approximately $750,000 needed to complete and evaluate the counseling service system would be allocated from the HUD research and technology budget.\textsuperscript{119}

As a result of this ragged history, there was in Fiscal Year 1974 no comprehensive system for assuring prospective homeowners such counseling as may have been needed to enable them to become effective homeowners. With the 18 month suspension of section 235 in effect, and a presidential policy of limiting domestic expenditures for overall economic reasons, Congress failed to make any counseling appropriation in 1973 for Fiscal Year 1974.

In 1972, Senator Percy proposed additional legislation to make explicit HUD's responsibility to assist the unsophisticated homebuyer. Reintroduced in 1973 as the Home Buyer and Home Owner Protection Act (S. 1614),\textsuperscript{120} Senator Percy's bill would amend section 518 of the National Housing Act. This section had been enacted in 1964\textsuperscript{121} to authorize the Secretary of HUD to pay for correcting structural defects in certain FHA-insured properties. In 1970, as a result of the adverse home ownership publicity, Congress added section 518(b) to authorize similar payments for "structural and other" aspects in the case of section 235 housing.\textsuperscript{122} S. 1614 would extend eligibility for compensation to all FHA programs, require a 3 year builder's warranty and allow a 5 year period for claims. In addition, the bill would create an Office of Consumer Assistance in HUD, authorize FHA neighborhood assistance offices, require additional seller/broker disclosures prior to closings, require annual reinspections for 5 years after initial insurance, and require a HUD-administered home ownership counseling program within 1 year after enactment.

The general provisions of the Percy bill have now become law, though in considerably less stringent form, in the Housing and Community Development Act of 1974.\textsuperscript{123} In addition, that Act amends the

HUD Act of 1968, that had authorized the Secretary of HUD to make technical assistance and front-end revolving loans available to nonprofit housing sponsors. Prior to the 1974 amendment, the law authorized “counseling on household management, self-help, budgeting, money management, child care, and related counseling services” to assist subsidized housing recipients in “improving their living conditions and housing opportunities, and in meeting the responsibilities of homeownership.” The 1974 amendment now makes this provision read “counseling and advice to tenants and homeowners with respect to property management, financial management, and such other matters as may be appropriate to assist them in improving their housing conditions and in meeting the responsibilities of tenancy and homeownership.” The Secretary was required to make such counseling available to section 235 homeowners. Whether this new provision, with its implied narrowing of the counseling focus to property and financial management, will be effective remains to be seen.

THE PROGRAM MORATORIUM, MOSKOW REPORT, AND HOUSING AND COMMUNITY DEVELOPMENT ACT OF 1974

In his celebrated—and in some circles notorious—address to the National Association of Homebuilders on January 8, 1973, HUD Secretary George Romney announced that the Nixon Administration had, as of January 5, imposed a suspension or moratorium on all subsidized housing programs. According to Secretary Lynn who took office shortly thereafter,

the suspension of the housing subsidy programs was necessary to avoid committing the Government to many additional billions of future dollars while we study alternative ways to better meet housing needs without the inequities, inefficiency and waste which has [sic] characterized these programs in the past.

In announcing the program suspension, the Department of Housing and Urban Development embarked on a massive, top-priority study of the programs involved, under the direction of Assistant Secretary Michael H. Moskow. The study, according to Secretary Lynn, was to focus on:

127. See note 21 supra.
First, the roles of government in housing and housing finance . . . .
Second, what should be the role of Government in housing and housing finance? Third, what changes in policy and programs are necessary to achieve the appropriate role of Government in housing and housing finance?\(^{129}\)

Over 80 full time employees were assigned to the study, in addition to numerous contractors and consultants. In his state of the Union message to Congress on community development on March 8, President Nixon pledged that policy recommendations would be made to Congress by September 7, 1973.\(^{130}\)

As noted above, the suspension and study received an enthusiastically negative reception on Capitol Hill.\(^{131}\) In his first appearance before the Senate Housing and Urban Affairs Subcommittee since his confirmation, Secretary Lynn was grilled relentlessly on the rationale for the program suspension and the schedule for delivery of the Administration's recommendations.\(^{132}\) When, for example, Secretary Lynn told Senator J. Bennett Johnston, Jr., Louisiana Democrat, that he hoped to be able to "be at least a long way toward the legislation" by the September 7 target date, Senator John Tower, a strongly pro-Administration Texas Republican, broke in to say pointedly, "I would suggest that it be in your best interest to have the legislation prepared at that time."\(^{133}\)

In a special message to Congress on September 19, President Nixon unveiled the long-awaited recommendations,\(^{134}\) purportedly based on the HUD study which was made public on October 6. After discussing proposals to ease the credit crunch and make long-term improvements in the credit system, President Nixon turned to "the challenge of low income housing."\(^{135}\)

"All across America," the President observed, "the Federal Government has become the biggest slumlord in history."\(^{136}\) The main flaw in the subsidized housing approach, he averred, was "its underlying assumption that the basic problem of the poor is a lack of housing rather than a lack of income . . . . [O]f the policy alternatives available, the most promising way to achieve decent housing for all our families at

\(^{129}\) **Hearings on Oversight on Housing and Urban Development Programs, supra** note 102, pt. 1, at 245.

\(^{130}\) **119 CONG. REC.** S4122 (daily ed. March 8, 1973).

\(^{131}\) **See pp. 6-7 supra.**

\(^{132}\) **Hearings on Oversight of Housing and Urban Development Programs, supra** note 102, pt. 1, at 249-67.

\(^{133}\) **Id.** at 251.

\(^{134}\) **119 CONG. REC.** S16,861 (daily ed. Sept. 19, 1973).

\(^{135}\) **Id.** at S16,863.

\(^{136}\) **Id.** at S16,864.
Citing a number of unresolved policy questions with respect to this approach, the President declared that they deserved "close examination," so that a decision could be reached in late 1974 or early 1975. Title I of the Administration's proposed legislation contained a formal endorsement of direct cash assistance, but only experimental authority.

Remarkably, close examination of the Moskow report revealed that it contained no discussion whatever of the direct cash assistance or housing allowance scheme! While experimental work on the concept had been under way for 3 years, involving a total projected expenditure of $168.8 million, the final results of all the housing allowance experiments were not expected until 1976 at the earliest.

Reaction to the presidential message of September 19 was predictably harsh. A New York investment bank newsletter observed:

Perhaps the greatest significance of the President's message last week lies in its insignificance . . . the failure to propose anything to fill the void between now and the 1976-77 implementation of allowances means that the Government role in the provision of low income housing will be nearly nil for several years.

At the more liberal end of the spectrum, the newsletter of the Movement for Economic Justice reported:

The President's new housing program offers immediate and substantial monetary benefits to housing investors. It offers middle America an opportunity to spend more money. The moderate and low income citizenry will have to wait to find out what it offers them. For the next 18 months they have been guaranteed a continuing study of their problems.

Senator William Proxmire, Wisconsin Democrat, a frequent and harsh critic of the Nixon Administration policy, described the September 19 message in a Senate speech: "[It is] not only a disappointment. It is a disaster." Ridiculing this "no policy" policy, Proxmire branded it a "cover-up for HUD's own mismanagement and in far too many cases, actually corruption." He accused Administration spokes-

137. Id.
138. Id.
140. DEPT. OF HOUSING AND URBAN DEVELOPMENT, HOUSING IN THE SEVENTIES (October 6, 1973).
142. For a detailed description of the housing allowance experiment, see Hearings on HUD-Space-Science-Veterans Appropriations for 1974, supra note 9, pt. 3, at 877-85.
men of "talking out of both sides of their mouths," characterized the policy as "cruel, brutal and harsh" and claimed that it condemns millions of American families to a tragic plight."

Senator Robert Taft, Jr., Ohio Republican, offered this more even appraisal:

[The Administration's proposal after months of study that the thrust of our housing program over the next two years be still another study, raised additional doubts about its commitment to eliminate America's remaining housing problems with all possible speed . . . a very skeptical [Senate Banking, Housing and Urban Affairs] Committee placed the burden of proof on the Administration's shoulders to submit convincing evidence that the old programs could not be made to work satisfactorily. Such evidence was never presented.]

With little guidance from the Nixon Administration, other than its interest in a special revenue sharing program for community development, Congress passed and President Ford signed the Housing and Community Development Act of 1974, containing a number of provisions relevant to housing strategy and the home ownership programs.

Despite a major effort by the Senate to rationalize and consolidate all FHA programs into a Revised National Housing Act, the Act ultimately passed settles for making numerous amendments to the existing mortgage credit assistance programs. Of particular interest was a new provision requiring federal housing assistance funds to be used in accordance with State and local housing assistance plans. This provision signals the end of the unrestricted Individual Opportunity Strategy. Under it, a municipality could require that public housing and interest credit programs be offered only in specified areas, presaging the resurrection of the Neighborhood Strategy proposed by the Percy-Widnall bill in 1967.

In the same vein, the Act adds two new subsections to the declaration of the national housing goal contained in the HUD Act of 1968.

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146. Id. at S18,130-31.
152. Id. § 213 (1974 U.S. CODE CONG. & ADM. NEWS 3292).
153. See note 47 supra.
That declaration had focused exclusively on the Production Strategy goal of 26 million new housing units over the decade 1969-79, 6 million of them for low and moderate income families. The new language begins to resurrect a Neighborhood Strategy approach, although it continues to lack any emphasis on the initiative of neighborhood people that had characterized the 1967 proposals:

(b) The Congress further finds that policies designed to contribute to the achievement of the national housing goal have not directed sufficient attention and resources to the preservation of existing housing and neighborhoods, that the deterioration and abandonment of housing for the Nation's lower income families has accelerated over the last decade, and that this acceleration has contributed to neighborhood disintegration and has partially negated the progress toward achieving the national housing goal which has been made primarily through new housing construction.

(c) The Congress declares that if the national housing goal is to be achieved, a greater effort must be made to encourage the preservation of existing housing and neighborhoods through such measures as housing preservation, moderate rehabilitation, and improvements in housing management and maintenance, in conjunction with the provision of adequate municipal services. Such an effort should concentrate, to a greater extent than it has in the past, on housing and neighborhoods where deterioration is evident but has not yet become acute.\textsuperscript{155}

The new Act also provides an explicit new authorization for the experimental housing allowance program, including a pointed requirement that the Secretary report to Congress with his findings by May, 1976.\textsuperscript{156} Finally, the Act includes the new provisions on counseling and protection of unwary homebuyers previously described.\textsuperscript{157} While these provisions are unquestionably important, the 1974 Act does not appear to signal any dramatic turn in national housing or home ownership policy, although it may later be regarded as having planted the seeds of some emerging new ideas along those lines.

CONCLUSIONS

As of mid-1974, the following conclusions and recommendations can be offered based on the experience of the preceding 6 years of the federal effort to encourage lower income home ownership:


\textsuperscript{156} Id. § 802 (1974 U.S. Code Cong. & Admin. News 3350).

\textsuperscript{157} See text accompanying notes 123-26 supra.
1. In Thousands of Instances Home Ownership for Lower Income Families Has Been an Outstanding Success.

During Fiscal Year 1975 it is estimated that assistance payments will be made on 504,000 section 235 units, at a cost of $372 million. Despite a high default termination rate—now over 10 percent nationally, the FHA 235 program has been of vast importance in housing nearly half a million American families in decent homes of their own. This is no mean achievement. While the weaknesses of the program come first to the eye, it is well to remember that the successes to date have outnumbered the failures by about nine to one.

2. Contrary to Various Apologies Offered by Administration Officials, Home Ownership for Lower Income Families Was Not an Uncharted Field in 1968.

Extensive testimony before congressional committees, plus the results of numerous publicly and privately sponsored projects across the country, constituted a virtually complete picture of the pitfalls and opportunities associated with lower income home ownership. There can be no excuse of ignorance for HUD officials although the tremendous emphasis on increasing housing production might be cited as a mitigating factor.


The bills under consideration, prior to President Johnson's 1968 message on the cities, envisioned no more than 200,000 home ownership units over a 3 year period—through a Neighborhood Strategy, in the case of Senator Percy's proposal, and through an Individual Opportunity Strategy, in the case of the proposals of Senators Mondale, Ribicoff, and Clark. By superimposing a goal of 6 million assisted units over the ensuing decade, the President and Congress created a situation pregnant with future peril. The combination of these high production goals, the deep interest subsidy, the special risk insurance fund, FHA's unfamiliarity with inner city areas, the relaxation of the "economic soundness" doctrine, and the absence of either congressional or FHA emphasis on homeowner preparation and protection, was a certain recipe for serious problems.

4. Having Enacted the Combination of Provisions in the 1968 Act,

159. See text accompanying note 8 supra.
Congress Failed to Follow Through on the Counseling It Had Advocated.

By rebuffing HUD's budget request for counseling funds in Fiscal Years 1970 and 1971, Congress not only made an effective counseling program impossible, but also gave HUD the impression that Congress did not think it as important as it had once stated. This was to have serious consequences.

5. Despite the Failure of Congress to Fund Counseling Programs, HUD Had Little Excuse for Abandoning Its Demands, and When Unexpectedly Granted Counseling Funds, Fumbling Their Utilization.

For 3 years, as the problems of lower income home ownership programs became more and more serious, HUD seemingly was unable to mount any effort to deal with the “people problems” involved. Secretary Romney made commendable efforts to tighten internal procedures and change negative attitudes within the department, but, as usual, FHA remained more interested in “units” and “insurance in force,” than in shepherding individual home buyers. And when Congress unexpectedly provided a counseling appropriation, HUD gave a strong impression of having little idea how to use it effectively.


For 8 years the federal government has pondered methods for coordinating its resources with those of State and local governments and private businesses and organizations to help lower income families achieve the goals of economic security and improved life opportunities. These methods have included the War on Poverty, Model Cities, Work Incentive Program (WIN), and Federal Regional Councils. Extensive studies have been undertaken on the subject, with the al-

most inevitable finding that the desired coordination and focusing of effort has only very rarely been achieved. This conclusion has been so clear-cut that it cannot have failed to have been a major influence in President Nixon's revenue sharing strategy. While revenue sharing in no way guarantees an effective integrated approach in solving these problems, it does have the effect of removing the federal government as the major actor, thus reducing by several the number of programs to be integrated locally.

Perhaps the greatest hope for achieving such an integrated approach, at least in urban areas, lies in reviving the Neighborhood Strategy. Local community development corporations\textsuperscript{166} and housing development corporations, or possibly local subunits of government, may well afford the brightest opportunity for achieving these goals.

7. A Neighborhood Strategy and a Production Strategy Are Necessarily in Conflict in Inner City Areas.

If reviving declining urban neighborhoods through an integrated, neighborhood-oriented approach is adopted as a major strategy, either at the national level or at a State or local level, it is highly unlikely that the housing goals of the 1968 Act can be thereby achieved. The fact is that moving forward on a broad front within an urban neighborhood, relying in considerable measure upon the talents and resources of neighborhood residents, is a slow, fitful process. As every developer and urban renewal administrator knows, the way to get housing units quickly is to bulldoze and build new construction, with little concern for the former inhabitants of the area. That kind of program clearly violates the Neighborhood Strategy.

This is not to say that the Neighborhood and Production Strategies are completely incompatible in all areas. Where there is no neighborhood—as in dispersed rural areas—the Production Strategy will work well so long as there are customers available. In urban neighborhoods characterized by rows of abandoned and decrepit housing and a few

\textit{The United States, 117 Cong. Rec. 7962 (1971); and Office of Management and Budget, Papers Relating to the President's Department Reorganization Program, chs. 3, 5 (February 1972).}

\textit{165. The State of the Union Address of the President of the United States, 117 Cong. Rec. 167-8 (1971).}

stable families, traditional bulldozing and rebuilding may be the only alternative to inaction. But a goal of empowering urban neighborhood people to revive and preserve their own neighborhoods is not a goal that can maximize housing production.

8. Housing the Lower Income Family Is Going to Continue to Cost The Taxpayer Money.

Liberalized building codes, amended zoning laws, technological and managerial breakthroughs, and the like may lower the cost of housing relative to the resources available to members of the lower income group. They may succeed in increasing their incomes through better jobs and increased productivity. But it is hard to conceive of hundreds of thousands of America’s lower income families enjoying decent housing in the larger urban areas without the public footing a substantial part of the bill through one device or another. The public has committed itself, for better or for worse, to accepting this burden on behalf of those unable to care for themselves in education, health, income, and housing; there is no cheap and easy way out of this responsibility.

ALTERNATIVE POLICIES

Having set forth these conclusions from the examination of the FHA lower income home ownership programs, it remains to consider alternative policies that might be adopted by Congress in this area.

Policy I: Revenue Sharing

President Nixon initiated a strong effort toward termination of categorical grant assistance programs in favor of general and special revenue sharing with State and local governments. While this approach has no particular merit in solving the ultimate problems, it does have the merit of relieving the federal government from any active responsibility for their solution. For this reason, of course, it is controversial.

Although at least one city (Fresno, California) has experimented with its own mortgage insurance program, it would seem unwise to terminate FHA and expect each state or locality to create its own mortgage insurance organization. There are two possibilities, however, that could build upon a revenue sharing approach to place the principal responsibility for improving housing at lower levels of government.

Under revenue sharing, housing subsidies could be terminated as federal programs, with FHA remaining as an unsubsidized mortgage insurance agency. FHA would agree to insure mortgages coinsured by State or local governments. Such a program might provide that whenever the default termination rate for the single family FHA program exceeded 3 percent of the insurance in force, in a participating state or municipality, that unit of government would be assessed the additional costs resulting from the defaults. This would maintain the mortgage insuring machinery of FHA intact, but require the State and local governments to exercise considerable care in coinsuring, and to provide any subsidy. If a given state wished to reap the benefits of a high housing production rate for lower income families, it would have to provide the subsidies out of its revenue sharing funds, and stand the risk of terminations resulting in assessments on it by FHA. Such a program would clearly involve a drastic reorganization of FHA and a major new involvement in housing by most State or local governments.

A second variation on this theme would involve private mortgage insurance companies, such as Mortgage Guaranty Insurance Company, headquartered in Milwaukee. A State or local government could agree to indemnify the reserve fund of such a private company, provided the company insured a specified number of families who would otherwise not be eligible for normal-risk insurance. The Wisconsin State Indemnity Fund, in fact, has since 1967 offered just such a program in that State.\(^\text{168}\) This type of program is analogous to the Nuclear Energy Liability Insurance Association,\(^\text{169}\) an association of private liability insurers formed to insure nuclear power stations against utterly unpredictable claims that might result from a major nuclear incident. NELIA is underwritten by the federal government in the event losses, to date nonexistent, exceed a specified dollar amount.

Under this variation, both the State and the private mortgage insurance company would have an economic interest to minimize the number of defaults.

**Policy 2: An Income Strategy**

This policy is exemplified by President Nixon's now defunct Family

\(^{168}\) Wisconsin State Indemnity Fund, ch. 609, Laws of Wisconsin, ch. 117, Laws of 1973. It has not, however, been widely used, reportedly due to lack of interest in inner city development.

Assistance Plan,\textsuperscript{170} the idea of housing allowances, now under intensive study at HUD, and the Negative Income Tax proposal of Dr. Milton Friedman\textsuperscript{171} Basically, this strategy eschews governmental assistance programs other than the provision of money to those without money. It affirms that the problem of lower income people is that they have little money; it prescribes the governmental provision of a sufficient amount of subsidy to poor people and the termination of all social service programs. According to this strategy, the poor know better than anyone else what is good for them, and if provided with money will purchase what they need, whether it is alcohol or night school.

The housing version of the income strategy is the housing allowance. Under this plan, the government gives eligible families a voucher redeemable in decent housing, either ownership or rental. It has the virtue of allowing the family to choose its own housing, rather than making assistance available only to those who are willing to live in certain kinds of housing in certain locations.

There are, however, grave problems with the housing allowance. An obvious one is that in a low-vacancy housing market a large infusion of housing allowance funds can only drive up the price of the existing housing. Since housing allowances are not made available on a contract basis covering the life of a typical housing mortgage, no builder or developer is likely to expand his construction because of the allowances. That is, where there is no assurance that Congress will not cancel the program next year, no reasonable home builder will commit himself to increasing the housing stock in anticipation of long term buying power that may well not materialize.

If this economic obstacle is resolved by providing for a long term allowance—say 20 years—then one of the problems that led to the housing allowance idea in the first place—the length of the assistance obligations involved in present public housing, 235 and 236, and rent supplement—reappears.

Congress will no doubt peruse the findings of the HUD housing allowance study with great care, for these reasons.

\textit{Policy 3: An Improved 235/236 Assistance Strategy}

In addition to the internal improvements instituted at FHA in response to the recent problems, there are a number of structural changes

\textsuperscript{170} H.R. 1, 92d Cong., 1st Sess. (1971).
that would improve the existing 235/236 mechanism. None of these changes, however, will relieve the Government from the responsibility for either purchasing and holding the mortgage itself for a number of years, as under the old BMIR programs, or contracting to make payments to a private mortgagee so long as the unit is occupied by an eligible family.

The first improvement to the 235 program would be the addition of a strong counseling and protection program for home buyers in advance of purchase and for a period thereafter. This has been discussed above, and the parameters are fairly well-known.

A second major improvement would be to replace the clumsy and burdensome income recertification procedure with a graduated income tax recapture system. Under this system, worked out in detail by a task force at Harvard’s Institute of Politics in 1968, FHA would pay a fixed monthly amount to the mortgagee over the lifetime of the mortgage. The occupant, whether owner or renter, would, however, file an additional statement with his annual federal income tax return. As his income rose, a graduated recapture surtax would be imposed to offset the fixed subsidy. At a specified level of income the surtax would completely cancel the federal payment, leaving the occupant completely unsubsidized. This method obviates any need for having the landlord, mortgagee, employer or FHA office certify the occupant’s income year after year.

In a further refinement of the idea, the amount of net subsidy (payment less surtax) paid each year would be accrued in what would amount to a revolving charge account in the Internal Revenue Service’s computers. For those occupants whose incomes rose to middle income or upper income levels, not only would the annual net subsidy decline to zero, but the surtax would continue to offset the accumulated subsidy from previous years. This would be true whether the occupant sold his subsidized home or vacated his subsidized apartment. For those whose incomes did not rise, of course, the payments would continue as a subsidy.

In addition to solving the awkward recertification problem, this plan would phase down the subsidy smoothly as incomes rose, and increase the subsidy in case family income dropped. It would ease the problem of inequity often cited by critics of the 235 program by permitting many

172. See discussion pp. 25-30 supra.
families to take part in the program, with widely varying subsidies, and confidentiality preserved. A careful study of the capacity of the Treasury's data processing equipment and procedures, made by IBM in 1967, revealed that the operating cost of maintaining such a system, once the initial information had been inserted, was ridiculously small.174

A third improvement in this category would be a limitation of the assisted housing programs to neighborhoods in which some public or private body has a continuing interest, i.e., an urban renewal, code enforcement, model cities neighborhood or Community Development Corporation (CDC) area. This would necessarily restrict the production opportunities, but it would almost certainly reduce the default rate and focus available program money on high-impact neighborhoods. The disadvantage of such a provision, absent a full fledged Neighborhood Strategy, is that it creates an invidious distinction among different urban areas and restricts individual opportunity to take advantage of the program wherever the individual desires to locate.

A fourth improvement would be the initiation of a home ownership equity insurance program. The Housing and Urban Development Act of 1968 directed the Secretary of Housing and Urban Development to report to Congress within 6 months his recommendations for an insurance program for protecting homeowners against defaults due to death, disability, and involuntary unemployment.175 This report is now 5½ years overdue, and Congress has seemingly lost interest.

This is regrettable. The late Professor Charles Abrams, long known as the dean of American housing, felt strongly that enactment of such an insurance plan, which he believed to be highly feasible, would be a "landmark in American housing legislation."176

There are, to be sure, problems involved in constructing a home ownership equity insurance program. These have been well outlined in a technical report prepared by the private insurance industry and submitted to HUD in 1969.177 The value and cost of a sound scheme of this kind will not be known until Congress insists that the Secretary of HUD discharge his responsibility under this neglected section of the 1968 Act.

174. Memorandum to the author from Ralph Hawes, Washington Representative, IBM, April 1967.
176. 1967 Senate Housing Hearings, supra note 28, at 717.
Policy 4: *A Full Fledged Neighborhood Strategy*

A full fledged Neighborhood Strategy would leave open the question of rural areas and of urban neighborhoods too far gone to be rescued. It would, however, in the remaining urban neighborhoods, attempt to marshal the talents and energies of neighborhood residents, along with increased knowledge and resources, to revive their neighborhoods and make them once again decent, wholesome, productive places in which to live.

The central role that housing policy might play in this neighborhood revival was extensively described by Senator Percy in 1967, in the explanation of his National Home Ownership Foundation Act of that year. But beyond mere housing programs, the concurrent programs for jobs, education, municipal services, transportation, beautification, and crime prevention would require a high degree of resource concentration and program coordination—a degree yet unachieved in any American city of any size.

Indeed, a Neighborhood Strategy is open to the charge that the neighborhood may no longer be the viable human community of the city. Secretary Romney, for instance, has argued strongly the case for dealing with the “Real City,” the metropolitan area, instead of subcities such as model city areas. While it is evident that an urban neighborhood cannot reasonably assume control of all transportation, sewage disposal, and police functions, there are nevertheless a number of functions that could lend themselves to neighborhood “mini-city” supervision. In fact, a combination of the “Real City” approach and the “mini-city” approach might come to supersede the present structure of a centralized city government, powerless neighborhoods, and governmentally unrelated suburbs.

A full fledged Neighborhood Strategy would only be attempted after extensive experimentation and hence a considerable time delay. The community development corporations funded under Title VII of the Economic Opportunity Act could offer useful vehicles, in coopera-

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180. *See note 166 supra.*
tion with a city government, for pioneering this approach. Using CDC's to test the concept would seem to be a useful approach.

**Policy 5: A Straight Out Production Strategy**

A straight out Production Strategy, if successful, would increase the housing supply to the point where lower income families would have increased choice in decent housing within their price range. This of course relies on the much abused trickle-down effect, where upper income families move into the new homes, and lower income families move up a notch into homes vacated by middle income families.

There is no reason, other than costs and overall economic policy, for not embarking on a responsible Production Strategy. But to be truly responsible, the Production Strategy cannot at one and the same time emphasize high production, low income families, relaxed mortgage requirements, a special risk insurance fund, and no support for unsophisticated homeowners. Instead, it can seek to increase overall housing production in areas favored by private market forces.

Elements of a Production Strategy would be: technological advances; new techniques of management and land assembly, typified by New York's Urban Development Corporation;\(^1\) new towns development; building code and work rule reform; lowering entry barriers to construction labor and contractors by ending restrictive union practices and onerous bonding requirements for contractors; and tax incentives to produce more of certain kinds of housing.\(^2\) Except for some foregone revenue in the case of tax incentives, much of this program could be undertaken at minimal economic cost to the Government, but, as can be seen by the nature of the elements listed, the political costs would not be inconsiderable. In addition, this strategy would not include any explicit commitment to creating housing for the poor; if past experience is any guide, criticism of the trickle-down approach to better housing would be intense from many organized interest groups.

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There may, perhaps, be additional policies which could be developed, but the foregoing would seem to be the most likely to emerge in one mixture or another.

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\(^2\) INT. REV. CODE OF 1954, § 167(k) allows a 60 month depreciation period and zero salvage value for specified rehabilitation expenditures for low income rental housing.
Barring a full scale commitment to an income strategy (Policy 2), wise policy would indicate a compatible blend of an improved 235/236 strategy (Policy 3), with special attention to rebuilding urban neighborhoods (Policy 4), using revenue sharing funds (Policy 1), in an overall climate of a responsible program for expanding production (Policy 5). Contriving such a blend will obviously require a serious effort. Yet the experience is available to construct such a policy blend. There are resources available, despite conflicting demands and overall economic problems. What has been missing so far is an eagerness to learn from experience, and to admit that much of the Gordian knot of urban housing is caused not by the intrinsic economics of housing production, but by the people problems of urban America, compounded by the nature of the public programs, laws, and regulations that define the ground rules for problem solving.

The events of the past 6 years have not signaled the death of the idea of home ownership for the aspiring and upwardly mobile poor family, or even, under certain circumstances, of the welfare family. They have, instead, made it clear what circumstances are requisite to the success of home ownership for lower income families. Knowing those circumstances, Congress can continue to help to make home ownership available to many thousands of Americans, as it pledged to do in the euphoric year of 1968.