NAHMAnalysis™
NATIONAL AFFORDABLE HOUSING MANAGEMENT ASSOCIATION

**Ensuring NAHMA Members Receive the Latest News and Analysis of Breaking Issues in Affordable Housing**

National Affordable Housing Management Association – 400 N. Columbus Street, Suite 203 - Alexandria, VA 22314
Phone 703-683-8630 - Fax 703-683-8634 - www.nahma.org

November 14, 2017 NAHMAnalysis 2017-1114

# Rural Rental Assistance Shortfalls 2013-2015: GAO Findings and Recommendations

In recent years, USDA's Rural Housing Service (RHS) has experienced funding gaps in its Rental Assistance program that created difficulties for property owners and tenants, including significant delays in rental assistance payments for fiscal years 2013-2015.

In response, the Government Accountability Office (GAO) compiled a report that examines the reasons for funding gaps and USDA's plans for improvement in the future, and concludes by laying out policy recommendations for the agency. This NAHMAnalysis summarizes the findings and implications of the GAO's report, titled "Rural Housing Service: Additional Actions would Help Ensure Reasonableness of Rental Assistance Estimates."

## Background: Why did GAO conduct this study?

Each year, USDA's Rural Housing Service (RHS) provides monthly rent subsidies for more than 280,000 households in approximately 15,000 properties financed by direct loans from RHS's Multi-Family Housing Direct Loans and Farm Labor Housing Direct Loans and Grants programs. With an annual budget of more than $1.3 billion, the rental assistance program is RHS's largest program and accounts for more than half of RHS's annual budget.

Under the Section 521 Rental Assistance Program, eligible low-income tenants pay up to 30% of their income toward rent, and RHS makes payments each month to the property owner to cover the balance. However, in fiscal years 2013, 2014, and 2015, RHS was not able to renew all eligible rental assistance agreements due to funding shortfalls prior to the end of the fiscal year (September 30), which resulted in missed or delayed rental assistance payments to owners.

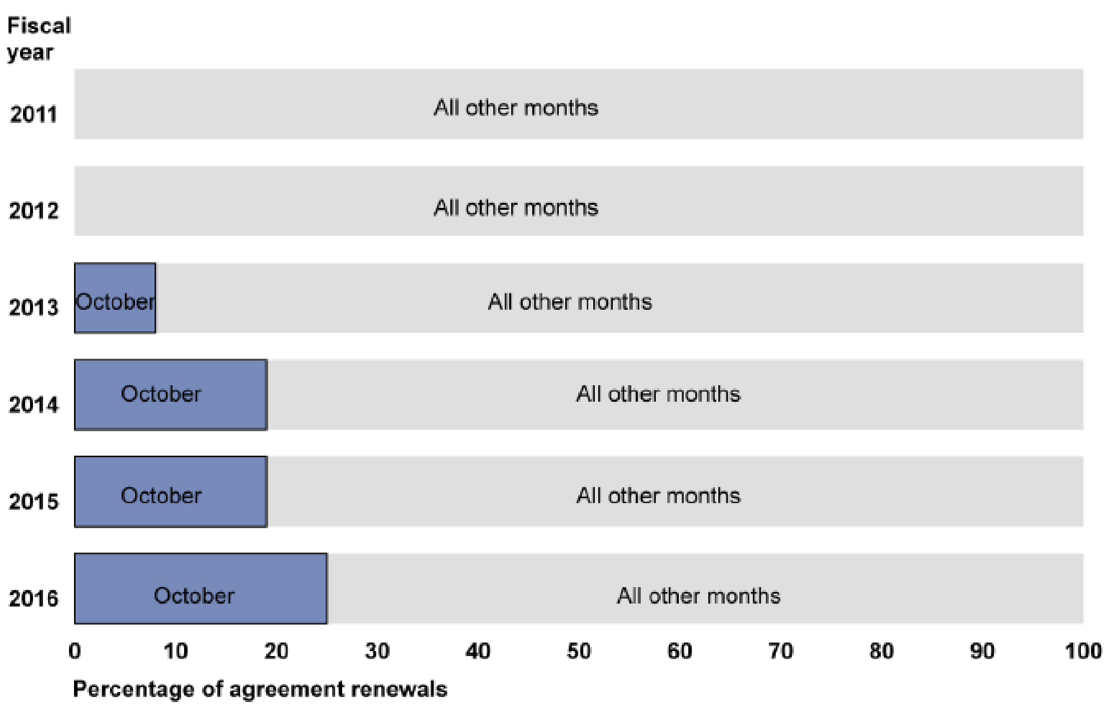
## Taking a closer look: What happened and why?

The nature of RHS's rental assistance agreements with owners offers insight into the funding shortfalls: RHS provides the rental subsidies through agreements with property owners for an amount estimated to last for 12 monthly regular assistance payments; the owners draw down on this amount each month until it is expended, at which time the agreement is automatically renewed if funding is available and the owner is in compliance.

In practice, however, the rental assistance agreements are unlikely to last for exactly 12 payments because of the uncertainty in estimating rental assistance costs: Many factors lead to rental assistance agreements lasting shorter or longer than anticipated, including changes to tenant incomes or unit vacancies and rehabilitations. Because agreements with owners expire when the original dollar amount is fully expended, and because of the inexact estimation of the annual agreement amount, the period covered by the agreements may last shorter or longer than 12 months, which can cause renewals to be triggered more than once per year.

Funding shortfalls leading to non-renewals can occur when overall agency funding is low, or when overestimated accounts tie up funds for accounts that fall short. Both of these scenarios occurred during fiscal years 2013, 2014, and 2015, leading to 1,652 property agreement non-renewals due to lack of funds over the course of three years. In response, the Senate Appropriations Subcommittee on Agriculture, Rural Development, Food and Drug Administration, and Related Agencies asked the GAO to investigate. RHS's report, titled "Rural Housing Service: Additional Actions would Help Ensure Reasonableness of Rental Assistance Estimate," was submitted to the Subcommittee on September 13, 2017.

**Figure 1: Percentage of RHS Rental Assistance Agreements Renewed in October Compared with the Rest of the Fiscal Year, Fiscal Year 2011-2016**




Source: GAO analysis of Rural Housing Service (RHS) data. | GAO-17-725

## Details of the study: Reasons for and responses to funding shortfalls

Following the budget shortfalls, the GAO was asked to examine reasons RHS ran out of funds for renewing rental assistance agreements in fiscal years 2013-2015, and how it responded, as well as what RHS has done to help prevent future funding gaps. In order to compile its report, the GAO analyzed RHS budget and rental assistance data for relevant years, reviewed RHS policies and procedures, and interviewed RHS officials and staff from national and randomly-selected state offices.

In its submitted report, the GAO found an interplay of three main factors contributing to USDA's funding gaps from 2013-2015:

- **Fiscal year 2013 sequestration and rescissions**
  In fiscal year 2013, sequestration and rescissions cut about $70 million of the rental assistance program's approximately $907 million budget; the GAO study found these cuts to have implications for 2014, as well, because renewals that could not be funded at the end of 2013 were pushed into the subsequent year. In fact, in each fiscal year, some or all of the agreements that could not be renewed on time due to funding gaps were renewed when the next fiscal year's appropriations became available; agreements renewed early in the year were more likely to need a second renewal later that year, further increasing the likelihood of funding shortfalls before the end of the fiscal year (figure 1).
- **Unreliable methods for estimating rental assistance costs and budget amounts**
  RHS's methods for calculating the dollar amount for annual renewal agreements and budget requests multiplied the number of rental assistance units by a state-wide, per-unit average cost; because actual costs at each property differed from the state average, this method proved inaccurate; specifically, the GAO report found that 64% of agreements renewed during the 3-year period lasted for less than or more than 11-13 payments. Additionally, RHS failed to account for "second renewals" (which occur when the same property requires two renewals of its rental assistance agreement in the same fiscal year) for two of the three years in question.
- **Limited management flexibility to navigate shortfalls**
  In addition to the challenges presented by constrained sequestration resources, RHS also faced challenges in addressing the renewal funding gaps because of program requirements. For example, because RHS's rental assistance agreements specify a dollar amount of funding that will be available for rental assistance at the property until fully expended, moving funds from agreements with more funds than needed for a 12-month period to agreements with a funding shortfall could have breached the agreements. Other mitigation strategies, such as authorization for RHS to enter into partial-year agreements, or an RHS ability to prioritize renewals for properties where the need might surpass that of other properties (based on vacancy and other rates) would have first required legislative authority; although RHS requested certain legislative changes, these proposals were generally not enacted.

The report also found that RHS's responses to the shortfalls in each of the fiscal years resulted in a combination of positive and negative consequences:

- **Options to lessen financial impacts on owners**
  Particularly in fiscal year 2013, RHS offered owners options to lessen the financial effect of missing rental assistance payments. For example, RHS offered owners the option to use money from the property's reserve account for operating purposes, suspend payments to the capital reserve account, and defer loan payments to RHS mortgages. However, owners who declined these options were not compensated for the missed rental assistance payments. Further, when some property owners chose to defer their mortgage payments at the end of 2013, RHS's automated accounting system incorrectly marked the owners as delinquent on their mortgages; in response, RHS waived late fees on those inaccurate delinquencies, and the RHS accounting system was eventually updated to create deferral transactions without delinquencies.
- **Prohibition on second renewals**
  In fiscal year 2015, RHS tried to decrease the likelihood of a funding gap by asking Congress to prohibit second renewals, which was meant to prevent the program from running out of funds for standard renewals. The GAO found this approach to put both owners and tenants in second renewal properties in financially difficult positions. In addition, because Congress enacted the prohibition about two and a half months into the fiscal year, the agreements entered into before that date were eligible for second renewals, resulting in close to 600 unanticipated renewals, which again led to a funding shortfall in fiscal year 2015. The prohibition was removed by Congress in fiscal year 2016.
- **Use of unexpected funds from properties that exited the program**
  In fiscal years 2014 and 2015, RHS funded agreement renewals with rental assistance funds previously obligated to properties that then exited the program due to mortgage prepayment, maturity, or foreclosure. However, when RHS uses funds obligated to properties that exited the program to address funding needs at other properties, those rental assistance "units" permanently leave the program. Therefore, the GAO concluded that a "trade-off of RHS's strategy is a shrinking portfolio of assisted rental units."

## Policy Implications: GAO Recommendations

In 2014, RHS began developing a rental assistance "obligation tool" to help improve and streamline rental assistance estimates and obligation processes. The model estimates RA costs based on each property's monthly requests over the previous year, but weighs more recent request amounts higher; the tool – which RHS began using for fiscal year 2016 renewals and the fiscal year 2017 budget estimate – also takes into account any recent or planned rent increases and new property information, and creates a mechanism for RHS to apply an inflation rate to forecasted program costs.

Overall, the GAO study found the new obligation tool to be an improvement over previous practices in that it reduces administrative burden on state office staff and improves the accuracy of the rental assistance agreement amounts: In fiscal year 2016, about 82% of rental assistance agreement durations fell within the 11-13 month timeframe.

However, the GAO did find some weaknesses with RHS's current approach, both regarding the obligation tool and with staff responsibilities at some Rural Development state offices: The GOA recommended further enhancements to the process to compensate for vacancy or rehabilitation scenarios which have led to a number of agreements lasting significantly longer than 12 months. In addition, the GAO noted the possibility of the obligation tool – which weighs more recent rental assistance usage more heavily – to incorrectly estimate renewal amounts for rental agreements at farm labor housing properties, where occupancy levels vary seasonally. Finally, the GAO found that RHS's estimates of second renewal amounts for its fiscal year 2016 budget request, which was completed before the obligation tool was activated, were substantially low, demonstrating the continued potential for misestimates that could create the kind of spill-over effects seen in previous fiscal cycles.

In addition, the GAO spoke with staff at 15 randomly selected RD state offices about their understandings of roles and responsibilities regarding rental assistance renewals. GAO concluded that some staff had differing understandings of their roles for reviewing the renewals; in addition, the staff understandings sometimes varied from the role set forth by the program officials in RHS's national office.

The following concerns and recommendations were highlighted in the GAO report:

- RHS lacks a plan for ongoing monitoring of its new obligation tool and has not always used the most relevant data. The GAO recommends that the RHS Administrator develop and implement a plan for ongoing monitoring.
- RHS has not incorporated automated checks into the obligation tool to mitigate the risks of misestimates and to improve compliance with the OMB requirement to use the President's inflation rates when compiling budget estimates; controls should be established (according to federal internal control standards) to check the reasonableness of rental assistance agreement amounts calculated by the tool and to assure compliance with inflation rate requirements.
- RHS lacks written guidance on the responsibilities of Rural Development (RD) state offices for reviewing rental assistance agreement renewals before obligating funds. The GAO recommends that the RHS Administrator provide guidance to RD state offices that specifies staff responsibilities with regard to reviewing a property's mortgage servicing status prior to obligating funds.

## Conclusion

Overall, the GAO concluded in their study that "while the agency took some steps to mitigate effects on property owners and improve its budget estimates, weaknesses remain in some of RHS's budget estimation and execution process." The GAO also noted that some weaknesses may exist in part because the estimate system is relatively new and continues to be refined. NAHMA will continue to work closely with RD property owners, RHS staff, and members of Congress as we navigate the policy implications of the report; as always, we will keep NAHMA members up-to-date on RHS's work to address the concerns and conclusions of the report.