

December 22, 2009

To: HUD Secretary Shaun Donovan, Deputy Secretary Ron Sims, Assistant Secretary John Trasviña, and Assistant Secretary Sandra Henriquez

Re: Analysis of Impediments to Fair Housing in HUD's Affordable Housing Programs

Prepared by the Civil Rights Task Force on Federal Housing Policy¹

This memorandum is presented in the spirit of HUD's required "Analysis of Impediments to Fair Housing" (used by HUD grantees throughout the country) to convey our recommendations on actions that HUD itself could take to address obstacles created by its own programs that make it unnecessarily difficult to provide housing in communities of opportunity. As HUD has recognized, federal housing programs have in many cases perpetuated conditions of racial and economic segregation – but at the same time, HUD programs have the potential to change the geography of opportunity in the nation's metropolitan areas. We believe that, pursuant to the Department's "affirmatively furthering" mandate, HUD must assess its contribution to segregation, and use its tools in new ways to promote sustainable, integrated communities throughout our metropolitan regions.

This analysis covers some key concerns regarding impediments to development of affordable housing in higher opportunity areas that are embedded in the way that HUD administers its programs. *Recommendations on the tenant-based voucher program will be submitted separately.*

As a threshold step, HUD should undertake an internal review of all HUD programs to assess the extent to which programs perpetuate, create, or permit racial segregation in metropolitan areas.

- Across program areas, staff should identify the regulatory and sub-regulatory policies and procedures that facilitate the efforts of HUD and its grantees and partners to expand housing options in low-poverty communities of opportunity where HUD-assisted housing, or voucher households, are under-represented, as well as those requirements that impede such efforts.

¹ The Civil Rights Task Force on Federal Housing Policy is a loose coalition of legal services, fair housing, and civil rights organizations seeking to reform federal low income housing policy to promote desegregation and access to opportunity for low income families of color. The analysis presented in this memorandum is specifically endorsed by the organizations listed on pages 9-10. Many of the points raised here are also reflected in the final report of the National Commission on Fair Housing and Equal Opportunity (December 2008).

- HUD should adopt a desegregation metric that assesses the degree to which each HUD housing program is becoming more or less segregated.
- HUD must communicate, in deed as well as word, that investments of HUD funds must expand affordable housing opportunities for low income, non-white families in high opportunity, low-poverty areas as at least an equal priority with investments in distressed minority communities. This means that, throughout the country, at least half of new affordable housing investment (including funds for rehabilitation) should be set aside for high-opportunity areas and should be affirmatively marketed to minority families and residents now living in distressed communities.² The remaining affordable housing development should be built as part of mixed-income developments.
- For HUD programs that involve a competitive application process (such as those subject to the SuperNOFA) or that require HUD review and approval (such as multifamily programs and public housing development), the program offices should adopt review and approval procedures that assure that HUD resources are not used to further segregation and are instead utilized to promote residential integration and deconcentration of poverty.
- In racially segregated regions, or regions where government-funded housing is geographically concentrated, HUD should work across programmatic “silos” with state and local jurisdictions to develop a strategy to desegregate housing across the region and open up opportunities for low-income families in higher-opportunity areas.³

We encourage HUD to solicit a variety of perspectives on *how*, not *whether*, HUD programs can be adapted to create a more equitable and inclusive geography of opportunity in our metro regions. As a starting point, we offer the following non-exhaustive list of impediments that we have observed and experienced in our work:

1) Total Development Cost (TDC) rules: It is widely recognized that the TDCs used in the public housing program are inadequate to develop housing to modern, market-competitive standards. This is a barrier to development in any location, but HUD has developed “work arounds” for mixed income projects in distressed areas, while failing to show similar flexibility for projects in higher opportunity areas.

- HUD encourages PHAs to obtain CDBG, HOME, LIHTC, and other non-public housing funds to fill the gap between TDCs and actual costs, and exempts these

² It is also important to recognize that the proportion of affordable housing spending in high opportunity communities needs to be significantly higher than 50% in jurisdictions that have a strong history of racial and economic segregation and concentration of assisted housing, and in jurisdictions in which central cities are relatively small compared to suburban populations.

³ For an example of this approach, see Dr. Jill Khadduri’s expert report in *Thompson v. HUD*, at www.prrac.org/projects/fair_housing_commission/atlanta/khadduri.pdf.

sources from the calculation of TDCs. HUD also routinely allows exceptions from TDCs for “extraordinary site costs” involving the costly remediation of site deficiencies (such as steep slopes) or environmental hazards. This policy makes it possible for PHAs and developers to build new public housing on a site that might otherwise be deemed undesirable or too costly to remediate. It is an approach that HUD could take for other elements of TDC policies that impede fair housing outcomes.

- HUD explains the relative lack of affordable housing in higher opportunity areas by pointing to higher land costs in these areas, but does not include the costs of acquisition of land or property in higher cost areas within its exception for “extraordinary site costs.” To fill the gap between actual costs and TDCs, the PHA or developer is then forced to obtain additional public funds, effectively giving the local jurisdiction (or state housing finance agency) a veto over the project.
- TDCs should be raised to better reflect actual costs of development, including the costs of acquiring sites in high opportunity areas, and soft costs related to zoning, permitting, and other local regulation that add expense to a project.⁴ In the public housing context, the Community Renewal Cost factor in the TDC should be based on actual costs of relocation, supportive services, and other supports provided to residents of the housing and the affected neighborhoods. Alternatively, in order to affirmatively further fair housing, HUD should treat the costs to acquire sites in desirable higher opportunity areas as “extraordinary site costs” as it currently does for costs related to remediation of geologically or environmentally undesirable sites.

2) HOPE VI and Mixed Finance Practices inhibit development of replacement housing in higher opportunity neighborhoods: It is HUD’s stated intention to use the HOPE VI program and mixed finance public housing approaches for a broad Choice Neighborhoods initiative encompassing multiple HUD programs. Indeed, for several years, appropriations legislation has authorized a multifamily program modeled on HOPE VI that allows an owner to move HUD-insured financing and Section 8 contracts from one site to another as part of a demolition and revitalization project. From a civil rights perspective, HOPE VI is a poor model for other programs. The HOPE VI program operates without governing regulations, and in recent years, HUD has adopted practices and policies that inhibit the use of HOPE VI to develop replacement housing except within the racially and economically concentrated sites and neighborhoods where most distressed public housing already exists. A balanced use of HOPE VI funds to replace public housing both on the original site and off-site in the broader housing market would expand housing choice, accommodate the broad range of tenant preferences, mitigate the loss of units on-site,

⁴ Exclusionary zoning, of course, is a key factor in raising the cost of land. HUD requirements that conditioned funding on the elimination of exclusionary zoning would effectively remove such artificial inflationary pressures, and would mean that less supplemental funding would be required to achieve affordability in areas of opportunity.

and would quite possibly be the most meaningful measure that HUD could undertake to affirmatively further fair housing.

- **HOPE VI scoring criteria do not give PHAs any meaningful incentive to produce replacement housing in off-site locations that would affirmatively further fair housing:** When public housing is demolished, as generally occurs in connection with a HOPE VI revitalization project, HUD and PHAs have a unique opportunity to decentralize the location of public housing and change the geography of public housing. However, HUD's HOPE VI scoring criteria provide only one point to reward inclusion of off-site replacement housing, and do not require that the location of the off-site housing actually further fair housing.
- **Stringent HOPE VI threshold requirements for site control make it difficult to replace units off-site:** The requirements of the HOPE VI NOFA for site control dissuade many PHAs or developers from even attempting to include off-site housing in a HOPE VI application. The FY 2009 NOFA, for example, requires a PHA to identify sites and provide evidence of site control for *every* off-site property included in any phase of a revitalization plan, *prior to and as a threshold condition for even applying for HOPE VI funds*. Thus, a PHA that affirmatively desires to expand housing opportunities to new areas (including areas outside the PHA's "jurisdiction") through the development of HOPE VI replacement housing must not only expend other funds to acquire site control before it knows whether its application will be funded, but also risks rejection of the entire proposal if the evidence of site control for any site is deemed insufficient. Site control requirements are a similarly a barrier in other HUD programs
- **HUD's HOPE VI policies actually provide an avenue for PHAs to avoid civil rights site selection criteria:** Civil rights site selection criteria ordinarily bar the acquisition or construction of assisted housing in distressed, racially and economically "impacted" neighborhoods, subject to certain exceptions that have often overwhelmed the rule. For the HOPE VI program, however, HUD devised a policy that entirely circumvents the civil rights site and neighborhood standards if the properties are deemed to be in the "same neighborhood" of an existing HOPE VI site. Moreover, in recent years, HUD has adopted a very expansive definition of "same neighborhood" that considers any location within a three-mile radius of the existing site to be deemed within the "same neighborhood." This policy is not codified in regulation and is not based on empirical evidence or any broadly accepted definition of "neighborhood" in the social science literature. In older cities, many different neighborhoods, often separated by natural or man-made boundaries, will be encompassed within this three-mile radius. This unauthorized exception to the public housing site and neighborhood standards only serves to perpetuate segregation and reconcentration of poverty in nearby neighborhoods and schools.

3) HUD’s approval process for public housing acquisition and development proposals is needlessly burdensome and inhibits PHAs from acquiring property in opportunity areas: HUD’s involvement in the minutia of the development process impedes the development of housing in competitive real estate markets. HUD requires a PHA to submit a formal proposal pursuant to 24 C.F.R. 941.303 and to obtain HUD approval before it can use HUD funds for a development projects. This means that a PHA cannot use the HOPE VI, Capital Funds, or Replacement Housing Factor Funds already allocated to it to purchase an existing home or building until HUD has reviewed and approved routine real estate documents, such as title insurance commitments and exceptions. For example, assume a PHA (or a development partner) wishes to acquire and rehab 25, 50, or 100 single-family properties as they become available on the market or through foreclosure. HUD will not approve the financing for such a project as a whole, nor will it allow public housing funds to be used until after the PHA has identified and obtained site control of specific properties. Thus, unless the PHA has a large sum of non-public housing funds available for acquisition of site control and can identify and place the entire package under contract at one time (which is unlikely for properties in competitive markets), it is required to purchase the properties in small packages (e.g. 3 to 10 at a time) using non-public housing funds and/or a line of credit, and then conduct “mini-closings” for each package and execute separate budgets and mixed finance amendments each time. In practice, this means that PHAs cannot be prepared to act with sufficient speed to acquire single family homes that are foreclosed upon or come on the market in desirable areas.

HUD should streamline its procedures to facilitate acquisition of scattered site properties in mainstream market-driven communities, and should allow pools of properties (including properties that have not yet been identified, but which meet certain general criteria, including location in communities of opportunity) to be financed with a single transaction.⁵ HUD should then focus its resources on big picture policy and civil rights issues, rather than the minute details of real estate transactions.⁶ Freed from the role of overseeing the details of local real estate transaction, HUD resources could more effectively be focused on civil rights compliance. For example, HUD should monitor the siting decisions made by recipients and grantees to ensure that housing activities supported by the public housing funds do not create or perpetuate segregation, and to assure that financing is used to affirmatively expand housing choice in high opportunity locations.

⁵ This is similar to the approach recommended by housing experts to support the acquisition of single family properties, including foreclosed properties now coming back on the market, and small apartment buildings. The Joint Center for Housing Studies of Harvard University, *America’s Rental Housing: The Key to a Balanced National Policy* 23 (2008).

⁶ While it is important that the documents and title work be correct, HUD commonly relies on certifications for much more weighty issues of compliance. It should similarly accept certifications or opinions of counsel from PHA real estate counsel.

4) Moving to Work (MTW) provides little or no relief from HUD oversight of the details of development while purporting to waive civil rights site selection standards: HOPE VI grants are not included in the MTW block grant and thus continue to be subject in all respects to detailed HUD oversight. In other respects, HUD has granted sweeping statutory and regulatory waivers, while retaining for itself the extensive oversight of the details of development projects, as described above. At the same time, HUD has waived federal oversight of site selection, granting sweeping waivers of the civil rights site selection standards adopted in response to *Shannon v. HUD* and the affirmatively furthering requirement of Title VIII. The obligation to assure compliance with civil rights laws, and the duty to affirmatively further fair housing are statutory requirements and may not be waived.

5) Barriers to the use of Project-based Vouchers (PBVs) to develop replacement housing in high opportunity areas: HUD provides both tenant protection vouchers and Replacement Housing Factor Funds (RHFF) to replace public housing units lost to demolition. The PBV program is especially suitable for off-site development in high opportunity areas and for including deep subsidy units in mixed income developments. Without a capital subsidy, such as RHFF, the borrowing power of a PBV alone is generally not sufficient to finance new construction or acquisition of replacement units in higher opportunity areas. Used in tandem, however, PBVs and RHFF can provide much of the capital financing and operating subsidy needed to develop both on and off-site replacement housing. There is currently no statutory prohibition on combining these sources. An earlier bar that precluded the use of PBVs together with public housing funds was repealed by Congress in 2001. Despite the repeal, however, HUD has refused to allow PBVs and public housing capital subsidies to be used together to develop off-site rental replacement units. Instead of erecting barriers to innovative methods of financing, HUD should encourage and reward PHAs and development partners that use available subsidy streams to mitigate the loss of demolished public housing. HUD should especially facilitate and incent PHAs to use these subsidy streams to create an inventory of replacement units in high opportunity areas.

6) Barriers to affirmatively furthering fair housing in the Neighborhood Stabilization Program: Subprime, often predatory, lending and high rates of foreclosure have been epidemic in Cleveland, Baltimore and other inner city neighborhoods across America for decades. The distinguishing feature of the on-going foreclosure crisis is that it has become substantially a suburban phenomenon. The crisis offers an opportunity to make vacant, foreclosed single family properties available for re-use as rental housing --- at costs below that of new construction --- in areas that are experiencing high levels of foreclosure, but are also relatively high opportunity areas. As the Treasury Department has recognized, REO properties offer PHAs and non-profits a source of units to accommodate large family households who often have difficulty security assisted housing and to disperse their concentrations of public and assisted housing.⁷ However, HUD failed in both NSP-1 and NSP-2 to encourage or require NSP recipients to take advantage

⁷ Community Development Insights, *Property Disposition, Exploring Different Approaches for Preserving Affordable Housing Opportunities*, Comptroller of the Currency, U.S. Department of the Treasury (March 2009) at 2.

of this opportunity to change the geography of affordable housing, and instead, imposed barriers.

- **Civil rights site selection standards are missing from NSP rules and guidance.** To the contrary, recipients are allowed to meet the program's very low income targeting requirement by providing rental housing solely or primarily in distressed areas -- the same areas where HUD assisted housing is already concentrated.
- **NSP rules and guidance do not require recipients to select properties in locations that will affirmatively further fair housing:** NSP rules and guidance do not require recipients to locate any rental housing targeted to very low income households in higher opportunity areas, even those opportunity areas that meet HUD's criteria for high foreclosure activity (a score of 18 on a scale of 0 to 20). HUD should require grantees to locate no less than half of the housing targeted to very low income households in higher opportunity areas and locations that will affirmatively further fair housing, and to affirmatively market the housing to households in high poverty, low opportunity areas.⁸
- **HUD has actually discouraged recipients from locating rental housing funded through NSP in higher opportunity areas even if those neighborhoods are experiencing high levels of foreclosures.** In the initial implementation of the NSP 1 and NSP 2 programs, HUD has scored applications in a way that has steered NSP rental housing investments into higher poverty neighborhoods – even though the statutory language does not require such targeting. Instead, HUD should provide encouragement, incentives and technical assistance for NSP activities that would enable PHAs and others to disperse public and assisted housing in high opportunity areas, especially for families with children. HUD should also make it clear to grantees that their NSP activities will be monitored to ensure that they affirmatively further fair housing.
- **HUD should exercise leadership in its disposition practices for FHA single family properties:** HUD can provide such encouragement, and set an example for private lenders, by making its own inventory of FHA disposition properties located in high opportunity areas available at nominal cost or a substantial discount to PHAs and non-profits that will re-use them as rental housing for very low income families.

7) HUD has limited up front grants to the footprint of the same site as the demolished/disposed FHA project: HUD's administration of the Up Front Grant (UFG) program offers another example of a program in which HUD has needlessly erected barriers to fair housing and development of affordable housing in high opportunity areas. Under this program, HUD provides capital grants of \$40,000 per unit to replace

⁸ As noted above, a significantly higher proportion of affordable housing in high opportunity areas may be appropriate given local demographics and the history of segregation in the jurisdiction.

subsidized units that are lost when HUD decides to demolish, rather than preserve, an FHA multifamily project with a HUD-held mortgage.⁹ Beginning in the early 2000s, HUD started limiting the availability of Up Front Grants to housing developed within the footprint of the demolished FHA project. This restriction was not reflected in regulations, and was not subject to notice and comment, but instead was apparently based on a reinterpretation of the governing statute. This change in interpretation resulted in a significant impediment to preservation and development of affordable housing in higher opportunity areas. If a locality wished to reduce density of a distressed project, or to redevelop it as mixed income, it could not obtain Up Front Grant assistance to replace the lost units elsewhere in locations that would affirmatively further fair housing. In situations where the FHA multi-family project was located in a stable, mixed income neighborhood, it set up a conflict between the policy of preserving housing in such areas and the desire to reduce density or improve the project's income mix. In other cases, the new policy provided an excuse for a locality that wished to eliminate affordable housing to do so.

8) Neither fair housing, nor the strategic preservation of affordable housing in high opportunity areas, have been part of the decision-making process in the Mark to Market program: Little is gained by development of affordable housing in high opportunity areas if HUD does not act aggressively to preserve the relatively few affordable housing developments already located in those areas. HUD's Mark to Market (M2M) program has been successful in preserving affordable housing and lowering subsidy costs. But overcoming concentrations of poverty and race -- by preserving properties in locations that do not have such concentrations -- has not been part of the design of M2M or its implementation.¹⁰ As a result, the properties that have been preserved tend to be in low-rent, high poverty, low growth areas, while properties that are likely to opt-out are those in higher opportunity areas.¹¹ HUD's decision-making process in the M2M program should positively consider the location of a property in a high opportunity area that will affirmatively further fair housing.

9) Failure to affirmatively promote integrated housing opportunities: In addition to the barriers to development of opportunity-based housing listed above, it is reasonable to also include policies that HUD has failed to adopt, that would promote more geographic balance in its housing development programs. Some of these steps would include:

- Reestablishing funding for regional housing planning funding that includes establishment of local fair share housing goals for all municipalities and counties within a metropolitan area;
- Efforts to eliminate local approval requirements for affordable housing development, including elimination of such requirements in HUD funded programs, and prohibition of such requirements by state housing agencies;

⁹ Currently, there are no appropriations for this program which was very active earlier in the decade.

¹⁰ Khadduri and Wilkins, *Designing Subsidized Housing Programs: What Have We Learned* 21 (Joint Center for Housing Studies, Harvard University, 2007),.

¹¹ *Id.* at 23.

- A strong “affirmatively furthering” regulation that measures HUD grantees on their progress to reduce segregation and promote integration and deconcentration, and that provides meaningful sanctions for grantees that fail to comply with fair housing goals;
- Revitalization of HUD affirmative marketing requirements to ensure that African American and Latino families (and other minority groups) have meaningful access to affordable housing developed in high opportunity areas;
- Renewed engagement with the Treasury Department to adopt civil rights regulations – including site selection guidance – for the LIHTC Program; and
- Significant financial incentives across the board to encourage and reward low income housing development (including scattered site and housing acquisition programs) in high opportunity communities.

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As we were recently reminded by the court in the *Anti-Discrimination Center v. Westchester County* case, building affordable housing is an important goal, but it is the *location* of affordable housing (and the opportunity of all applicants to live there, through affirmative marketing, and fair housing enforcement and education programs), that determines whether that affordable housing promotes fair housing choice or merely perpetuates segregation. If HUD wants to begin to balance its housing policies by developing assisted family housing outside areas of minority concentration and higher-poverty schools, it will need to seriously reexamine its own programs and policies. HUD grantees, PHAs, and private developers cannot do this job on their own.

Philip Tegeler
Poverty & Race Research Action Council
Washington, DC

John Payton
NAACP Legal Defense Fund
New York, NY

Shanna L. Smith
National Fair Housing Alliance
Washington, DC

Joseph Rich
Lawyers’ Committee for Civil Rights Under Law
Washington, DC

Elizabeth Julian
Inclusive Communities Project
Dallas, TX

Susan Goering
ACLU of Maryland
Baltimore, MD

Craig Gurian
Anti-Discrimination Center
New York, NY

Fred Freiberg
Fair Housing Justice Center
New York, NY

Kevin D. Walsh
Fair Share Housing Center
Cherry Hill, NJ